

University of Warwick institutional repository: <http://go.warwick.ac.uk/wrap>

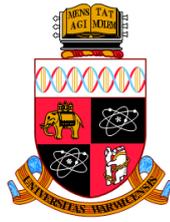
A Thesis Submitted for the Degree of PhD at the University of Warwick

<http://go.warwick.ac.uk/wrap/65045>

This thesis is made available online and is protected by original copyright.

Please scroll down to view the document itself.

Please refer to the repository record for this item for information to help you to cite it. Our policy information is available from the repository home page.



THE UNIVERSITY OF
WARWICK

**A Critique of Creative Shari'ah Compliance in the
Islamic Finance Industry with Reference to the Kingdom
of Saudi Arabia and the United Kingdom**

By

Ahmad Alkhamees

A thesis submitted in partial fulfilment of the requirements for the award
of a Degree of Doctor of Philosophy in Law

Supervisor

Professor Dalvinder Singh

The School of Law, University of Warwick
April 2014

Contents

| | |
|---|--------------|
| Acknowledgements | vi |
| Declaration..... | viii |
| Abstract..... | ix |
| Glossary of Arabic Terms | x |
| Abbreviations | xiv |
| Table of Cases..... | xvi |
| List of Statutes..... | xvii |
| List of Tables | xviii |
| List of Figures..... | xviii |
| Introduction..... | 1 |
| Defining Shari‘ah Compliance | 6 |
| Research Questions | 7 |
| Research Justification | 8 |
| Addressing the Lack of Research..... | 8 |
| Maintaining Financial Stability..... | 10 |
| Protecting Consumers | 11 |
| Mitigating Legal Risk | 12 |
| Boosting Economic Efficiency | 13 |
| Scope of the Study | 13 |
| Methodology | 14 |
| Structure of the Thesis | 15 |
| Chapter One: An Overview of Shari‘ah | 18 |
| 1.1. Introduction..... | 18 |
| 1.2. Overview of Shari‘ah and Its Foundation..... | 18 |
| 1.3. Schools of Thought | 20 |
| 1.4. Islamic Legal Ruling..... | 21 |
| 1.5. Main Features of Islamic Finance..... | 24 |
| 1.5.1. Ribā..... | 24 |

| | | |
|--------|--|----|
| 1.5.2. | Gharar | 26 |
| 1.5.3. | Maisir and Qim'ar | 27 |
| 1.6. | Shari'ah-Compliant Financial Instruments | 28 |
| 1.6.1. | Equity-Type Contracts..... | 29 |
| 1.6.2. | Debt-Financing Contracts..... | 30 |
| 1.7. | The Objectives of Islamic Law | 32 |
| 1.8. | Conclusion | 40 |

Chapter Two: The Form Versus Substance Debate and the Roots of Creative Shari'ah Compliance in Islamic Finance: Why Reinvent the Wheel? 41

| | | |
|--------|---|----|
| 2.1. | Introduction..... | 41 |
| 2.2. | The Definition of <i>Hilah</i> | 43 |
| 2.3. | The Origins and the Evolution of <i>Hilah</i> | 45 |
| 2.3.1. | The Excessive Use of Hypothetical Cases | 46 |
| 2.3.2. | Political Conflicts and State Oppression | 48 |
| 2.3.3. | The Gap between Shari'ah Ideology and Society's Needs..... | 49 |
| 2.3.4. | Positions on <i>Hilah</i> of Islamic Schools of Thought | 51 |
| 2.4.1. | The Shāfi'ī School | 52 |
| 2.4.2. | The Ḥanafī School | 56 |
| 2.4.3. | The Mālikī School | 59 |
| 2.4.4. | The Ḥanbalī School | 60 |
| 2.4.5. | Other Schools of Thought..... | 61 |
| 2.5. | Refuting the Pro- <i>Hilah</i> Arguments..... | 64 |
| 2.6. | Conclusion | 72 |

Chapter Three: *Tawarruq* as a Case Study of Creative Shari'ah Compliance 74

| | | |
|--------|---|----|
| 3.1. | Introduction..... | 74 |
| 3.2. | Definition of <i>Tawarruq</i> and Selection Rationale..... | 74 |
| 3.3. | The Development of <i>Tawarruq</i> | 76 |
| 3.3.1. | Jurisprudential <i>Tawarruq</i> | 77 |
| 3.3.2. | Partly Organised <i>Tawarruq</i> | 77 |
| 3.3.3. | Fully Organised <i>Tawarruq</i> | 77 |
| 3.4. | The Differences between Jurisprudential and Organised <i>Tawarruq</i> | 80 |

| | | |
|---|--|------------|
| 3.5. | Forms of <i>Tawarruq</i> | 81 |
| 3.6. | Shari‘ah Jurists’ Views on <i>Tawarruq</i> | 83 |
| 3.6.1. | Jurisprudential <i>Tawarruq</i> | 83 |
| 3.6.2. | Arguments against Organised <i>Tawarruq</i> | 84 |
| 3.6.3. | Arguments Supporting Organised <i>Tawarruq</i> | 90 |
| 3.6.4. | Is <i>Tawarruq</i> Better than <i>Ribā</i> ? | 94 |
| 3.7. | Conclusion | 96 |
| Chapter Four: Standardisation of <i>Fatwas</i> to Reduce Creative Shari‘ah Compliance | | 98 |
| 4.1. | Introduction..... | 98 |
| 4.2. | Standardisation: A Definition | 99 |
| 4.3. | Why Is Standardisation Needed? | 100 |
| 4.3.1. | Arguments for Standardisation..... | 100 |
| 4.3.2. | Arguments against Standardisation | 105 |
| 4.4. | Causes of Juristic Differences..... | 109 |
| 4.4.1. | Variable Quranic Recitations..... | 112 |
| 4.4.2. | Using Words with Multiple Meanings | 113 |
| 4.4.3. | Lack of Knowledge of Ḥadīth..... | 114 |
| 4.4.4. | Different Requirements for Adopting Ḥadīth..... | 116 |
| 4.4.5. | Adopting Certain Legal Principles | 118 |
| 4.4.6. | Disregarding the Change of <i>Maṣlaḥah</i> | 120 |
| 4.4.7. | The Structure of the <i>Fatwa</i> Question..... | 122 |
| 4.5. | Remedies for Inconsistency | 123 |
| 4.6. | Conclusion | 132 |
| Chapter Five: The Impact of Shari‘ah Governance Practises on Shari‘ah Compliance in Contemporary Islamic Finance | | 133 |
| 5.1. | Introduction..... | 133 |
| 5.2. | Shari‘ah Supervisory Board Definition | 134 |
| 5.3. | The Importance of SSBs | 136 |
| 5.4. | Regulatory Issues Surrounding Shari‘ah Supervisory Boards..... | 139 |
| 5.4.1. | The Ambiguous Role of SSBs..... | 139 |

| | | |
|--|--|------------|
| 5.4.2. | SSBs' Lack of Legal Status | 147 |
| 5.4.3. | SSBs' Lack of Accountability | 153 |
| 5.4.4. | SSBs' Lack of Transparency | 159 |
| 5.4.5. | The Lack of Independence of SSBs | 165 |
| 5.4.6. | Conflicts of Interest | 179 |
| 5.4.7. | Lack of Competence | 189 |
| 5.5. | Conclusion | 194 |
| Chapter Six: Public Mechanisms to Remedy Creative Shari'ah Compliance ... | | 196 |
| 6.1. | Introduction..... | 196 |
| 6.2. | Overview and Justification of CSSBs..... | 196 |
| 6.2.1. | Justifications for CSSBs | 198 |
| 6.3. | Tasks of CSSBs..... | 201 |
| 6.4. | The Central Shari'ah Board in Sudan | 203 |
| 6.5. | The Central Shari'ah Board in Malaysia | 206 |
| 6.5.1. | BNM Shari'ah Governance Framework for Islamic Financial Institutions..... | 210 |
| 6.6. | UK Regulators' Approach towards Shari'ah Governance..... | 215 |
| 6.7. | Saudi Regulators' Approach towards Shari'ah Governance | 226 |
| 6.8. | Compulsory Disclosure..... | 237 |
| 6.9. | Conclusion | 242 |
| Chapter Seven: Private Mechanisms to Remedy Creative Shari'ah Compliance | | 245 |
| 7.1. | Introduction..... | 245 |
| 7.2. | Shari'ah Compliance Rating | 246 |
| 7.3. | Shari'ah Indices | 253 |
| 7.4. | Private External Shari'ah Auditing Firms..... | 255 |
| 7.5. | International Islamic Financial Standards..... | 260 |
| 7.6. | Whistle Blowing | 266 |
| 7.7. | Characterising the Articles of Association | 268 |
| 7.8. | Conclusion | 269 |
| Conclusion | | 271 |
| Bibliography | | 285 |

Acknowledgements

Gratitude is due to Allah, The Most Compassionate and The Most Merciful, for giving me patience, strength, and ability to complete this study.

I would like to express my gratitude and heartfelt thanks to my distinguished supervisor, Professor Dalvinder Singh, for his valuable guidance, encouragement, time, and sincere efforts during the course of my research.

My gratitude also goes to Mr Nicholas H. D. Foster, Dr Musa Usman Abubakar, Dr Abou Jeng, Sheikh Faizal Ahmad Manjoo, Salim Al-Ali, and Khiled Al-Muflih for their inspiring comments and encouragement.

I would like also to thank my former and current colleagues at Warwick Law School, including Shahbaz A. Cheema, Rajnarah Akhtar, Rumana Islam, Joy Malala, Sheharyar Hamid, Hassan Nizami, and Pedro Florencio. Raza Saeed deserves special mention for his help and support.

My heartfelt gratitude goes to my parents and my siblings for their sacrifice, encouragement, and prayers for my success. I must extend special gratitude to wife, Reem, and my children, Hassan and Judy, who accompany me through this journey, never failing to provide me with love and warmth, and have helped to ease the pressure of the task of completing this thesis.

Dedication

To my dear parents: Abdullah Alkhamees and Moday al-shamssan

Declaration

I hereby declare that this thesis is my own work and effort. Where other sources of information have been used, they have been acknowledged. It has not been submitted in any previous application for any degree apart from an early version of the background material in sections 1.1 and 1.2 of chapter one, which was developed during the study of my arbitration module in my LLM degree and was published during the study of my PhD as:

- Alkamees, Ahmad. “International Arbitration and Shari'a Law: Context, Scope, and Intersections.” *Journal of International Arbitration* 28, no. 3 (2011): 255–64.

In addition, I have published the following parts of this thesis:

- An early version of chapter four was presented at “Business in between Cultures—The Development of Islamic Finance” in Sarajevo on 15 and 16 November 2012, and the conference proceedings is to be published by the European Association for Banking and Financial History.
- An early version of chapter five was published under the following citation: Alkamees, Ahmad. “The Impact of Shari’ah Governance Practises on Shari’ah Compliance in Contemporary Islamic Finance.” *Journal of Banking Regulation* 14, no. 2 (10 September 2012): 134–63.

Abstract

Creative Shari‘ah compliance can be defined as compliance with the letter but not the objectives of Shari‘ah. In recent years, Islamic finance industry practises have come under scrutiny, with strong critiques levelled against many institutions that claim to provide Shari‘ah-compliant Islamic financial products and services, while such products and services in fact undermine the spirit and the objectives of Shari‘ah. Financial instruments based on the profit- and loss-sharing model are deemed by Shari‘ah scholars and Muslim academics to be the most compliant with the objectives of Islamic law. Nonetheless, research has shown that they are the least practised forms of Islamic finance; in contrast, institutions offering Islamic financial services (IIFS) offer mainly debt-based instruments.

While many researchers have noted this gap between the theory and practise of Islamic finance, no study has provided a sustained analysis of the issue. This thesis undertakes such analysis and, in doing so, significantly contributes to the sphere of Islamic finance in three main ways. First, it critically appraises justifications of creative Shari‘ah compliance practises. Second, it examines how Shari‘ah supervisory board (SSB) governance practises and the inconsistent *fatwas* (Islamic legal opinions) issued by SSBs contribute to the issue of creative Shari‘ah compliance in contemporary Islamic finance. Most importantly, it suggests regulatory mechanisms which regulators can employ in Islamic countries such as Saudi Arabia and in secular countries such as the United Kingdom to deal with the issue of creative Shari‘ah compliance.

This thesis concludes that creative Shari‘ah compliance is not a phenomenon new to Islamic law, but it is one that has no solid justification in Islamic jurisprudence. This study suggests two public mechanisms to remedy the issue of creative Shari‘ah compliance: establishing central Shari‘ah supervisory boards and enforcing compulsory disclosure. In addition, it proposes private mechanisms to remedy creative Shari‘ah compliance which can be employed without governmental involvement. These mechanisms include adopting a Shari‘ah compliance rating, Shari‘ah indices, private Shari‘ah auditing, international standards related to enhancing Shari‘ah compliance, and a whistle-blowing policy for serious Shari‘ah-compliance violations, as well as characterising an IIFS in its articles of association as an entity that fully complies with Shari‘ah ruling. These remedies are particularly useful when an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari‘ah governance.

Glossary of Arabic Terms

'*adl*: justice

'*adālah*: upright character

aḥād: single

ahl al-ḥadīth: An Islamic school of thought started mainly in Medina; “the traditionalists”

ahl al-ra'y: An Islamic school of thought in Iraq; literally “the people of good sense”

al-ḍarūrāt tuqaddir biqadarihā (legal maxim): what is permitted due to necessity is restricted to times of necessity

al-ḍarūriyāt tubīḥ al-maḥzūrāt (legal maxim): necessity legalises prohibitions

al-faḍal: an excess

al-jam': when two different opinions are declared jointly valid for applications in different times or conditions

al-kirā': lease

al-nsa': a delay

al-qirāḍ: silent partnership

al-ṣiḥḥah: the notion of validity

al-siyāsah al-shar'iyah: Shari'ah-based policy or politics

al-tawarruq al-Mubark: the blessed *tawarruq*

al-umwr bimaqāṣidihā (legal maxim): acts are judged by intentions

'*Amal Ahl al-Madīnah*: the established practise of the people of Medina

'*aqidah*: dogma

'*aql*: intellect

bai' al-'ina: a form of finance where an owner sells his asset on a deferred basis, then buys it back from the purchaser on a cash basis at a price that is usually lower than the original selling price

bay' al-dyn: the selling of debt

bay' al-talji'h: fictitious or temporary sale used to avoid seizure by unjust rulers

dar' al-mafṣadah: preventing harm

ḍarūriyāt: the necessities

dīn: religion

fāsīd: void

fatwa: Islamic legal opinion

fiqh: Islamic jurisprudence

fiqh al-mu'āmalāt: Islamic commercial jurisprudence

gharar: risk or uncertainty

ḥadīth: traditions of the Prophet; see *sunnah*

ḥājiyyāt: the complementary; the needs

ḥīlah: legal ruse

ḥisāb: account

ḥisbah: the Islamic notion that individual Muslims have a duty to command right behaviour and forbid wrongdoing to keep society in line with the teachings of Islam

ḥiyal: plural of *ḥīlah*
ḥukum: judgement
‘ibādāt: rituals
‘iddah: a legal waiting period before the women can remarry
ijārah: leasing
ijmā’: consensus
ijtihād: a reasoning process that Islamic jurists use to determine how Shari‘ah law applies to a particular case
īnah: double sales
istiḥsān: juristic preference
istiqrā’: inductive reading
jalb al-maṣlaḥa: achieving a benefit
madhhab: schools of thought
maisir: gambling
makhraj fiqhī: jurisprudential leeway
makrūh: discouraged
māl: wealth
māni’: hindrance
maqāṣid: objective
maqāṣid al-sharī‘ah: the objectives of Islamic law
maqāṣid ‘āmmah: general objectives
maqāṣid khāṣṣah: specific objectives
marāḍ al-mawt: the time of death-sickness
maṣlaḥah: public interest
maṣlaḥah mursalah: public interest
mastahab: recommended
mubāḥ: neutral or indifferent
mudarib: entrepreneur or trustee of a venture
mudd ‘ajwah: where two *ribawī* items are exchanged and one of them includes an additional item of a different sort
muftī: a scholar who provides a Shari‘ah answer
muḥarram: prohibited
muḥtasib: a person conducting *ḥisbah*
mujtahid: a person who practises *ijtihād*
mukallaf: religiously accountable person
murābahah: a mark-up sale
mushārahah: partnership
mushtarak: homonymous or semantically ambiguous
mustaftī: an individual who seeks a *fatwa* to answer his question
mutawātir: consecutive
nafs: life
nasl: posterity
nikāḥ al-taḥlīl: a formalistic contract allowing a woman to remarry a former husband after three divorces

qawl al-sahābī: interpretation or the *fatwa* of a companion of the Prophet
qim'ar: a game of chance
qurū': time
qyās: analogy
ribā: “usury” or “interest”, but with a wider meaning in Shari‘ah
ribā al-buyū': the usury of trade
ribā al-faḍal: the usury of surplus
ribā al-nasī'ah: the usury of delay
ribā al-qurūd: the usury of loans
ribawī: usurious
sabab: a cause
ṣadaqah: obligatory charity tax
sadd al-dhariā'i: precautionary legal prohibition
ṣaḥiḥ: valid
ṣaḥiḥ diyānatan: religiously permissible
ṣaḥiḥ qaḍā'an: judicially valid
shart: condition
shuf'ah: pre-emption
ṣukūk: Islamic bonds
ṣukūk al-ijārah: lease-based *sukūk*
sunnah: the accumulation of the teachings of Prophet Muhammad, which includes his sayings, actions, decisions, and implicit approbation or disapproval of things
tadlīs: fraud
taḥsīynāt: luxuries
takaful: Islamic insurance
takhrīj: a process where in the absence of an opinion from the founding scholars on the case in question, a jurist either derives an opinion from a ruling of the school's founder on a different case or uses his legal methodology to derive an opinion from the original sources of Shari‘ah
talfīq: amalgamation or fusion of different legal opinions
Tāsh Mā Tāsh (television show): *No Big Deal*
tawarruq: a form of finance where buyer A purchases a commodity from a seller for a deferred payment and then resells it to buyer B for cash at a price that is usually lower than the original cost
tawriyah: misleading double entendres
tazkiyah: accrediting a witness by trustworthy person
'ulamā': scholars
'ur: custom
uṣūl al-fiqh: the principles of Islamic jurisprudence
wa'd: promise
wājib: obligatory
waqf: charitable endowment
wuḍū': ablution
zakāh: obligatory charity tax, one of the five pillars of Islam

ẓanni: speculative

ẓayd akhū 'ubayda (Arabic idiom): cut from the same cloth

Abbreviations

AAOIFI: Accounting and Auditing Organization for Islamic Financial Institutions
AGM: annual general meeting of shareholders
AH: After Hijra (Islamic calendar)
AIFA: Association for Islamic Finance Advancement
BNM: Bank Negara Malaysia
CDIFS: Committee of Developing Islamic Financial Services
CE: Common Era
CEO: Chief Executive Officer
CIBAFI: General Council for Islamic Banks and Institutions
CIDD: Combined Initial Disclosure Document
CSSB: Central Shari‘ah supervisory board
DJIMI: Dow Jones Islamic Market Index
EMP: Emphasis of Matter paragraph
FCA: Financial Conduct Authority
FSA: Financial Services Authority
GCC: Gulf Cooperation Council
HSSB: Higher Sharia Supervisory Board for Banks & Financial Institutions
IAIB: International Association of Islamic Banks
IFC: Islamic Finance Council UK
IFI: Islamic financial institution
IFSB: Islamic Financial Services Board
IFSB-10: IFSB Guiding Principles on Shari‘ah Governance Systems
IFSB-3: IFSB standard on Corporate Governance
IFSB-4: IFSB standard on Transparency and Market Discipline
IFSB-9: IFSB Guiding Principles on Conduct of Business for Institutions Offering Islamic Financial Services
IIBI: Institute of Islamic Banking and Insurance
IIFS: institution(s) offering Islamic financial services
IIRA: Islamic International Rating Agency
INCEIF: International Centre for Education in Islamic Finance
IOSCO: International Organization of Securities Commissions
ISRA: International Shari‘ah Research Academy for Islamic Finance
KSA: Kingdom of Saudi Arabia
MCB: Muslim Council of Britain
MCOB: UK Conduct of Business Sourcebook

MSE: Matters of Shari‘ah Emphasis
OIC: Organisation of the Islamic Conference
PLS: profit- and loss-sharing
RDR: Retail Distribution Review
SAC of the SC: Shari‘ah Advisory Council of the Securities Commission
SAC: Shari‘ah Advisory Council of [entity]
SAFs: private Shari‘ah auditing firms
SAIFS: Saudi Authority for Islamic Financial Standards
SAMA: Saudi Arabian Monetary Agency
SC: Securities Commission of Malaysia
SCFF: Supreme Commission for Financial Fatwa
SCFs: Shari‘ah consulting firms
SEC: Securities and Exchange Commission
SSB: Shari‘ah supervisory board
UAE: United Arab Emirates
UK: United Kingdom

Table of Cases

UK

Investment Dar Co Ksc V Blom Developments Bank Sal [2009] EWHC 3545 (CH)

Shamil Bank Bahrain V. Beximo Pharmeticals Limited & Ors [2003] EWHC 2118

Egypt

*The Supreme Constitutional Court of Egypt (Scc) 1994 Case No. 13 of Year 15,
12/1/1995*

List of Statutes

UK

Company Directors Disqualification Act 1986
Consumer Protection from Unfair Trading Regulations 2008
Financial Services Act 2002
Financial Services Act 2012
Fraud Act 2006

UAE

Federal Law No. 6 of 1985 Concerning Islamic Banks and Financial Institutions and Investment Companies

Saudi Arabia

The Basic Law of Governance. Royal Order No. (A/91), 1 March 1992
Capital Market Law. Royal Decree No. (M/30), 2003
Implementing Regulations of the Law on Supervision of Finance Companies (2013)
Charter of the Saudi Arabian Monetary Agency. Royal Decree No.23, 15 December 1957

Sudan

The Banking Business Organisation Act (2003)

Yemen

Act 21 (1996) as Amended by Act 16 (2009) on Islamic Banks in Yemen

Malaysia

Act 701 - Central Bank of Malaysia Act, 3 September 2009
Act 67 - Civil Law Act 1956
Capital Markets and Services Act 2007
Act 498 - Securities Commission Act 1993

Lebanon

Law No. 575, dated February 11, 2004 - the Establishment of Islamic Banks in Lebanon

Jordan

Law No. 28 of 2000

Kuwait

Law No. 32, 1968
Law No. 30, 2003

Syria

Monetary and Credit Council [Mcc], Admission Rules of Ssb of Islamic Banks Operating in the Syrian Arab Republic 404, Mn, B4.

List of Tables

| | |
|---|-----|
| Table 1. Shari‘ah Governance Disclosure Indexes in KSA Banks..... | 163 |
| Table 2. Shari‘ah Governance Disclosure Indexes in KSA Banks..... | 164 |
| Table 3. Top 10 SSB Members Worldwide..... | 180 |
| Table 4. IFSB Shari‘ah Governance Disclosures | 242 |
| Table 5. Shari‘ah Quality Rating | 251 |
| Table 6. IIRA Rating..... | 252 |

List of Figures

| | |
|--|----|
| Diagram 1. Jurisprudential <i>Tawarruq</i> | 79 |
| Diagram 2. Organised <i>Tawarruq</i> | 79 |
| Diagram 3. Inter-bank placement | 81 |
| Diagram 4. Inter-bank placement | 82 |
| Diagram 5. Reverse <i>Tawarruq</i> | 83 |

Introduction

Over the past few decades, the Islamic financial services industry has witnessed a rapid increase in size, with an annual growth rate of 10% to 20%.¹ Currently, more than 300 Islamic financial institutions (IFIs) are spread over 51 countries around the world.² Standard & Poor's estimates that the industry is worth approximately \$1.4 trillion,³ a number projected to reach \$2.8 trillion by 2015.⁴ These market figures have motivated a number of global financial institutions such as Citibank, Goldman Sachs, HSBC, and BNP Paribas to start offering Shari'ah-compliant financial services.⁵

However, claims have arisen that many institutions offer Shari'ah-compliant financial services which in practise appear to risk undermining the spirit and objectives of Islamic finance.⁶ This fear has been increasingly echoed by Shari'ah

¹Siba Sami Ammari, "Islamic Finance Industry Exceeds Growth Expectation as Conventional Finance Suffers through Economic Crisis," AME Info FZ LLC / Emap Limited, <http://www.ameinfo.com/218528.html>. accessed 12 September 2011. For the growth of Islamic finance industry worldwide see: M. Mansoor Khan and M. Ishaq Bhatti, "Islamic Banking and Finance: On Its Way to Globalization," *Managerial Finance* 34, no. 10 (2008).

²Juan Sole, "Introducing Islamic Banks into Conventional Banking Systems," (2007) *IMF Working Paper No. 07/175*(2007) <http://ssrn.com/abstract=1007924> accessed 12 September 2011.

³Zeynep Holmes and Surinder Kathpalia, "Standard & Poor's Islamic Finance Outlook 2014," http://www.standardandpoors.com/spf/upload/Ratings_EMEA/IslamicFinanceOutlook_2014.pdf. accessed 6 March 2014.

⁴Dana El Baltaji and Haris Anwar, "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance," Bloomberg, <http://www.bloomberg.com/news/2010-11-23/shariah-scholar-on-more-than-50-boards-opposes-limit-plan-islamic-finance.html>. accessed 25 November 2010.

⁵Dahlia El-Hawary, Wafik M. Grais, and Zamir Iqbal, "Regulating Islamic Financial Institutions : The Nature of The Regulated," *World Bank Policy Research Working Paper 3227, March 2004*(2004) [http://www-](http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2004/06/03/000009486_20040603173425/additional/112512322_20041117151025.pdf)

[wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2004/06/03/000009486_20040603173425/additional/112512322_20041117151025.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2004/06/03/000009486_20040603173425/additional/112512322_20041117151025.pdf) accessed 10 December 2010.

⁶ Refer to : Mahmoud Amin El-Gamal, *Islamic Finance : Law, Economics, and Practice* (Cambridge UK: Cambridge University Press, 2006), p12 & 23; Yahia Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking* (Hoboken, N.J.: Wiley, 2010), P237; Khalid Howladar, "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance," Moody's,

http://eng.assaif.org/content/download/7643/43051/file/MDYs_ShariahRisk_KHowladar.pdf. accessed 17 October 2010; Habib Ahmed, "Maqasid al-Shari'ah and Islamic Financial Products: A Framework for Assessment," *ISRA International Journal of Islamic Finance* 3, no. 1 (2011): p150; Tawfique Al-Mubarak and Noor Mohammad Osmani, "Applications of Maqasid al-Shari'ah and Maslahah in Islamic Banking practices: An Analysis" (paper presented at the International Seminar on Islamic Finance in India, Kochi, India, 4 - 6 /10/ 2010), p15; Houssemeddine Bedoui and Walid Mansour,

scholars, academics, and investors with particular interest in Islamic finance.⁷ For instance, Sheikh Saleh Kamel,⁸ one of the principal architects of the Islamic finance industry and the chairman and founder of many Islamic banks, lamented in a recent interview that many so-called Islamic banking products and services are not actually Islamic.⁹ Similarly, in 2008, the *sukūk* (Islamic bond) market suffered a loss of about \$15 billion in the wake of a renowned scholar's remark that 85% of the *ṣukūk* traded in the market are not Shari'ah compliant.¹⁰ This phenomenon is so prevalent that in 2011,¹¹ a popular Saudi Arabian television comedy called *Tāsh Mā Tāsh (No Big Deal)* provoked a huge controversy after accusing Islamic banks of being no different from conventional banks. The episode was titled *zayd akhū 'ubayda*, an Arabic idiom that means "cut from the same cloth". Moreover, the issue has been openly discussed in various newspapers which characterise the practise of institutions offering Islamic financial services (IIFS) as *tadlīs* (fraud).¹² Khan suggests that an IIFS "replaces

"Islamic banks performance and Maqasid alShari'ah" (paper presented at the the 9th Asia-Pacific Economic Association Conference, Osaka, Japan, 27-28/7/2013), p25..

⁷ See for example: A Fayyad, 'alerqabh alesher'eyh walethedyat alem'easerh ' Umm Al Qura University, HG Rammal, 'The Importance Of Shari'ah Supervision In Islamic Financial Institutions' (2006) 3 Corporate Ownership and Control Journal 204.

⁸ Saleh Kamel is the chairman of Dallah al Baraka Group in addition to the General Council for Islamic Banks. He has been involved in the Islamic finance industry and promoting Islamic economic research since 1969. In 2010, Malaysia awarded Saleh Kamel the Royal Award for Islamic Finance, acknowledging his leadership and personal commitment in promoting the global accessibility of Islamic finance. Mohd Syazwan Rahimy Mohd Mokthar, "Malaysia Honours Shaikh Saleh Abdullah Kamel," Vocus, <http://www.prweb.com/releases/2010/11/prweb4727694.htm>. accessed 23 September 2011.

⁹ Wael Mahdi, "Most of Islamic Financial Products are not Islamic," ArabianBusiness.com <http://www.arabianbusiness.com/arabic/517729>. accessed 10 November 2010.

¹⁰ Sara Hamdan, "Non-Sharia Compliance Costs sSukuk Industry Billions," The National, <http://www.zawya.com/Story.cfm/sidZAWYA20090414051357/Non-Sharia%20Compliance%20Costs%20Sukuk%20Industry%20Billions>. accessed 6 October 2010; Mohammed Khnifer, "\$ 31 Billion evaporate in 2008 after Osmani's Statements and the Financial Crisis", *Alaqtadyh Newspaper*, 17 January 2009 http://www.aleqt.com/2009/01/17/article_185096.html. accessed 10 October 2010.

¹¹ Alarabiya, "ḥalaqah zayd akhū 'ubayd fī ṭāsh 18 takshif wasā'il al-bunūk al-islāmiyah fī al-taḥāul biālribā," Alarabiya.net, <http://www.alarabiya.net/articles/2011/08/11/161888.html>. accessed 21 April 2012.

¹² See for example, Hend Al-Ahmad, "al-ghāmidī: ghālibiyh al-qanawāt al-maṣrifīyah al-slāmīyah lā tuṭabq mabādi al-āqtiṣād al-slāmī", *Alsharq Newspaper* 30/1/2012 <http://www.alsharq.net.sa/2012/01/30/104076>. accessed 1 May 2013; Mohammad Shoeb, "Present Islamic banks no different from other banks, experts lament", *Peninsula Newspaper*

conventional banking terminology with terms from classical Arabic and offers near-identical services to its clients but at a higher cost”.¹³ Bedoui and Mansour note that the Islamic finance industry “is simply the same conventional industry but with makeup”.¹⁴ The issue has even been noted by anti-Shari‘ah campaigners such as David Yerushalmi.¹⁵ In 1999, the US Office of the Comptroller of the Currency (OCC) reviewed and approved *murābahah* (a mark-up sale), the most common product offered by IIFS, concluding that “the economic substance of the *murābahah* financing transaction is functionally equivalent to either a real estate mortgage transaction or an inventory or equipment loan agreement”.¹⁶

The gap between the theory and the practise of Islamic finance has been pointed out by many researchers¹⁷ and characterised by some as constituting a kind of “Shari‘ah arbitrage”¹⁸ or “pseudo-Islamic product”.¹⁹ In theory, financial instruments which are based on the principle of profit- and loss-sharing (PLS) are the ideal form of financing in Islamic law.²⁰ However, IIFS offer primarily debt-based instruments,²¹

<http://thepeninsulaqatar.com/news/qatar/176705/present-islamic-banks-no-different-from-other-banks-experts-lament>. accessed 3 May 2012

¹³Feisal Khan, "How 'Islamic' is Islamic Banking?," *Journal of Economic Behavior & Organization* 76, no. 3 (2010): p818.

¹⁴Bedoui and Mansour, "Islamic banks performance and Maqasid alShari‘ah," p25.

¹⁵D. Yerushalmi, "Shari'ah's ``Black Box": Civil Liability and Criminal Exposure Surrounding Shari'ah-Compliant Finance," *Utah law review.*, no. 3 (2008).

¹⁶Office of the Comptroller of the Currency (OCC), "Interpretive Letter #867," OCC., <http://www.occ.gov/static/interpretations-and-precedents/nov99/int867.pdf>. accessed 1 May 2014

¹⁷ See for example , M. Fahim Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," *Thunderbird International Business Review* 49, no. 3 (2007): p287; Mohammed Nejatullah Siddiqi, "Banking and Finance in Theory and Practice: A Survey of the State of the Art," *Islamic Economic Studies* 13, no. 2 (2006): p1; Mehmet Asutay, "Conceptualisation of the Second Best Solution in Overcoming the Social Failure of Islamic Finance: Examining the Overpowering of Homoislamicus by Homoeconomicus," *IUM Journal of Economics and Management* 15, no. 2 (2007): p173; Zubair Hasan, "Fifty Years of Malaysian Economic Development: Policies and Achievements," *Review of Islamic Economics* 11, no. 2 (2007); Humayon A. Dar and John R. Presley, "Lack of Profit Loss Sharing in Islamic Banking: Management and Control Imbalances," *International Journal of Islamic Financial Services* 2, no. 2 (2000); Nikan Firoozye, "Wa'd and the completeness of Islamic markets," *Opalesque Islamic Finance Intelligence*, <http://www.kantakji.com/media/7540/c69.pdf>. accessed 5 May 2013.

¹⁸El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p21.

¹⁹Ahmed, "Maqasid al-Shari‘ah and Islamic Financial Products: A Framework for Assessment," p155.

²⁰Refer to: Abdulazeem Abozaid and Asyraf Wajdi Dusuki, "The Challenges of Realizing Maqasid al-Shari‘ah in Islamic Banking and Finance" (paper presented at the IIUM International Conference on

which Shari‘ah actively discourages.²² The permissibility of several heavily used financing instruments in the industry, such as *tawarruq*, *bai' al-'ina*, and *murābahah*,²³ is strongly disputed, as many Shari‘ah scholars see them as incompatible with the objectives of Islamic finance.²⁴ These transactions have been vilified as opening a “back door” to usurious prohibited transactions.²⁵

The practise which this thesis calls “creative Shari‘ah compliance”, drawing on the term “creative compliance” coined by McBarnet and Whelan,²⁶ starts when a *hīlah* (legal ruse) is employed to circumvent Islamic finance rules and thus to provide *fatwa*

Islamic Banking and Finance: ‘Research and Development: The Bridge between Ideals and Realities’, Kuala Lumpur, 23rd – 25th April 2007), p4-5; Muhammad Taqi Usmani, *An Introduction to Islamic Finance* (The Hague: Kluwer Law International, 2002), p12; Siti Faridah Abd Jabbar, "Sharia-Compliant Financial Instruments: Principles and Practice," *The Company Lawyer*. 30, no. 6 (2009): p179; Al-Mubarak and Osmani, "Applications of Maqasid al-Shari‘ah and Maslahah in Islamic Banking practices: An Analysis," p7.

²¹ See: Syed Abdus Samad, Norman D Gardner, and Bradley J Cook, "Islamic Banking and Finance in Theory and Practice: The Experience of Malaysia and Bahrain," *The American journal of Islamic social sciences*. 22, no. 2 (2005): p79; Nus Sechafia et al., "What Drives An Ideal Islamic Finance? A Maqasid Compliance Approach" (paper presented at the International Business and Social Sciences and Research Conference, Cancun, Mexico., 16 - 17 /12/ 2013), p11-13; Ezry Fahmy Eddy Yusof, Jhordy Kashoogie, and Asim Anwar Kamal, "Islamic Finance: Debt versus Equity Financing in the Light of Maqasid al-Shari‘ah.," (2009) <http://mpira.ub.uni-muenchen.de/id/eprint/20722> accessed 10 February 2014; Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p287; Siddiqi, "Banking and Finance in Theory and Practice: A Survey of the State of the Art," p1; Asutay, "Conceptualisation of the Second Best Solution in Overcoming the Social Failure of Islamic Finance: Examining the Overpowering of Homoislamicus by Homoeconomicus," p173; Hasan, "Fifty Years of Malaysian Economic Development: Policies and Achievements.,"; Dar and Presley, "Lack of Profit Loss Sharing in Islamic Banking: Management and Control Imbalances."

²² While Shari‘ah does not prohibit taking on interest-free debt, it actively discourages Muslims from taking on excessive debt. For instance, the Prophet often recites a prayer seeking refuge from sins and debt. In another incident, he refuses to lead the funeral prayer of person who died indebted and did not leave any money to repay the debt. See: Habib Ahmed, "Defining Ethics in Islamic Finance: Looking Beyond Legality " (paper presented at the 8th International Conference on Islamic Economics and Finance, Doha, 18th December 2011).

²³ For an explanation of *tawarruq*, *bai' al-'ina*, and *murābahah*, refer to chapter one, p30. For a summary of the contemporary discussion on *murābahah*, refer to Umar F Moghul and Arshad A Ahmed, "Contractual Forms in Islamic Finance Law and Islamic Inv. Co. of the Gulf (Bahamas) Ltd. v. Symphony Gems N.V. & Ors.: A First Impression of Islamic Finance," *Fordham International Law Journal* 27, no. 1 (2003): p174.

²⁴ Muhammad Ayub, *Understanding Islamic Finance* (Hoboken, NJ: John Wiley & Sons, 2007), p475; Mohammad Nejatullah Siddiqi, "Economics Of Tawarruq: How Its Mafasid Overwhelm The Masalih," http://www.siddiqi.com/mns/Economics_of_Tawarruq.pdf. accessed 8 August 2011; Nikan Firoozye, "Tawarruq: Shariah Risk or Banking Conundrum?," *Opalesque Islamic Finance Intelligence*, http://www.opalesque.com/OIFI12/Featured_Structure_Tawarruq_Shariah_Risk_or_Banking438.html. accessed 09 December 2010; Ahmed, "Maqasid al-Shari‘ah and Islamic Financial Products: A Framework for Assessment," p150.

²⁵ Al-Mubarak and Osmani, "Applications of Maqasid al-Shari‘ah and Maslahah in Islamic Banking practices: An Analysis," p2.

²⁶ Doreen McBarnet and Christopher Whelan, "The Elusive Spirit of the Law: Formalism and the Struggle for Legal Control," *The Modern Law Review* 54, no. 6 (1991).

(Islamic legal opinion) that suits the institution's products, regardless of the fact that these products blatantly contravene the spirit of Islamic law. Creative Shari'ah compliance might involve restructuring conventional products in a way that satisfies Shari'ah requirements in form but not in substance.²⁷ This revised structure usually consists of multiple complex contracts and sub-agreements branded with Arabic names.²⁸ The aim of these combined contracts is "breaking down the overall questionable transaction into two segments—each of which, individually, being Shari'ah compliant—whose combination ends up recreating the overall effect of the forbidden transaction".²⁹ The complexity of such an instrument sometimes makes it hard for experts to verify its compliance with Shari'ah law.³⁰ This procedure has been called "Black Box Syndrome" by Shaykh Yusuf Talal DeLorenzo,³¹ an American Shari'ah scholar and a renowned figure within the industry. He writes:

I would like to see more faith in what true and diligent Shari'ah compliance actually means to our industry. I am dismayed by quick fixes and shortcuts which in many cases circumvent the Shari'ah. The industry has proved time and again that adherence to the principles of Shari'ah can be profitable, and that such adherence does not spell hardship. We have no need of "black boxes" and of arm's length transactions that miraculously produce results by sacrificing the spirit of the Shari'ah to the letter of the law.

The deployment of creative compliance practises to avoid standards is not a new phenomenon, especially in relation to standards of practise in accounting and

²⁷Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p237.

²⁸ See: Reza Djojosugito, "Mitigating Legal Risk in Islamic Banking Operations," *Humanomics* 24, no. 2 (2008): p111; Khan, "How 'Islamic' is Islamic Banking?," p818.

²⁹Osama Athar, "An Outsider's View on Islamic Finance", Harvard Islamic Finance Forum", *Dinar Standard*TM, <http://www.dinarstandard.com/finance/HarvardFin051908.htm>. accessed 10 November 2011; see also: Ahmed, "Maqasid al-Shari'ah and Islamic Financial Products: A Framework for Assessment," p150.

³⁰Howladar, "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance".

³¹Yusuf Talal DeLorenzo, "The Black Box Syndrome: A New Challenge for Shariah Supervisory Boards," *Islamic Finance news*, <http://www.shariahunds.com/pubs/news/Islamic%20Finance%20News%20V4i14.pdf>. accessed 11 March 2014.

taxation³² as well as in various legal areas such as environmental law³³ and labour law.³⁴ McBarnet and Whelan distinguish between “rule compliance”, which adheres only to the letter of the law, and “substantive compliance”, which is compatible with the law’s overall objectives.³⁵ While creative compliance does not impugn the validity of the standard of practise in conventional finance, it does run the risk of making contracts and agreements void in Islamic finance,³⁶ which would pose a greater legal risk than conventional finance.

Defining Shari‘ah Compliance

The term “Shari‘ah compliance” has no standard definition;³⁷ different authors have used it to refer to different concepts. For instance, Mikail and Arifin³⁸ describe as “Shari‘ah compliant” those financial products which have origins in conventional finance but have been “Islamised”, while they use “Shari‘ah-based” to refer to products which have no foundation in conventional finance. On the other hand, Ahmed³⁹ uses “Shari‘ah compliance” to refer to products which conform to the form and substance of Shari‘ah but not to the social needs of the community, while using the term “Shari‘ah-based” to refer to products which conform to the form and

³²McBarnet and Whelan, "The Elusive Spirit of the Law: Formalism and the Struggle for Legal Control." See also: Doreen J. McBarnet, *Crime, Compliance and Control* (Aldershot: Ashgate/Dartmouth, 2004).

³³Daniel A. Farber, "Taking Slippage Seriously: Noncompliance and Creative Compliance in Environmental Law," *Harvard Environmental Law Review* 23, no. 2 (1999).

³⁴Amanda Pyman, "Creative Compliance in Labour Relations: ‘Turning the Law on its Head’," in *Advances in Industrial & Labor Relations*, ed. David Lewin and Bruce E. Kaufman (Emerald Group Publishing Limited, 2005)

³⁵Karen Yeung, *Securing Compliance : a Principled Approach* (Oxford: Hart Pub, 2004), p11.

³⁶ See: Djojosingito, "Mitigating Legal Risk in Islamic Banking Operations."; Sole, "Introducing Islamic Banks into Conventional Banking Systems". p4.

³⁷Sa'id Adekunle Mikail and Mahamad Arifin, "A Critical Study on Shari'Ah Compliant and Shari'Ah Based Products in Islamic Banking Institutions," *Journal of Islamic and Human Advanced Research* 3, no. 4 (2013): p169.

³⁸Ibid.

³⁹Ahmed, "Maqasid al-Shari'ah and Islamic Financial Products: A Framework for Assessment," p156.

substance of Shari‘ah and satisfy “the legitimate needs of all market segments”,⁴⁰ including small entrepreneurs and the poor. In this thesis, the term “Shari‘ah compliance” refers to substantive compliance with the form and collective goals of Islamic law.

Research Questions

This research seeks to engage with the following questions:

- Is creative Shari‘ah compliance a phenomenon new to Islamic law? Are the positions of the various Islamic jurisprudential schools supporting “substance” or “form” in Islamic finance? Does Islamic jurisprudence justify using *hīlah* (a legal ruse) to practise creative Shari‘ah compliance?
- To what extent do inconsistencies in the *fatwas* issued by Shari‘ah supervisory boards (SSBs) contribute to the issue of creative Shari‘ah compliance? What are the causes of juristic differences? Will standardisation of Shari‘ah rulings benefit or harm the Islamic finance industry? How did Islamic states deal with this issue in the past, and is there justification in Islam for enforcing a particular view of one school of thought?
- Are SSB governance practises affecting Shari‘ah compliance in IIFS? Specifically, how could issues such as SSBs’ unclear functions and legal status, lack of accountability and transparency, and conflicts of interest and lack of independence, as well as the poor training and inadequate qualifications of SSB members, contribute to the issue of creative Shari‘ah compliance in the contemporary Islamic finance industry?
- To what extent can a national body be involved in addressing the issue of creative Shari‘ah compliance? Should states establish a central Shari‘ah

⁴⁰Ibid.

supervisory board (CSSB)? What are the limitations of a CSSB as a public mechanism to deal with creative Shari'ah compliance? Do the regulatory approaches toward Shari'ah governance that are applied in the United Kingdom (UK) and the Kingdom of Saudi Arabia (KSA) adequately deal with creative Shari'ah compliance?

- What role can the private sector play in remedying creative Shari'ah compliance? Specifically, how effective are private mechanisms such as adopting a Shari'ah compliance rating, Shari'ah indices, a whistle-blowing policy for serious Shari'ah-compliance violations, and private Shari'ah auditing in dealing with creative Shari'ah compliance? Can these remedies be used when an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari'ah governance?

Research Justification

The rationale for undertaking this research is fivefold, in that the study addresses the lack of research in this subject as well as the need to maintain financial stability, protect consumers, mitigate legal risk, and boost economic efficiency in the Islamic financial industry.

Addressing the Lack of Research

Shari'ah compliance is the backbone of Islamic finance, yet not much attention has been paid to the issue of creative Shari'ah compliance from a regulatory perspective. The existing literature has identified the issue but stopped short of profoundly analysing it or addressing key factors which contribute to the phenomenon.⁴¹ Research in Islamic finance has disproportionately focused on issues of agency theory in Islamic investment accounts, corporate governance, and Shari'ah

⁴¹ For example, refer to the sources mentioned in footnote 17.

board practises, while devoting little time to issues and challenges of creative Shari‘ah compliance.⁴² My study remedies the paucity of research in this area by critically appraising justifications of creative Shari‘ah compliance practises and examining the relationship between SSB governance practises and creative Shari‘ah compliance in contemporary Islamic finance. It also offers researchers who do not read Arabic critical access to the classical and present-day discourse of Shari‘ah scholars.

Most importantly, the thesis suggests regulatory mechanisms which can be employed by regulators in Islamic countries such as Saudi Arabia and secular countries such as the United Kingdom to deal with the issue of creative Shari‘ah compliance. The choice of Saudi Arabia is motivated by the fact that despite the huge and growing market for Islamic finance, regulation of the industry is nonexistent, as there are neither the legal instruments nor an appropriate body to oversee the industry. In fact, as Rodney Wilson⁴³ has observed, “The sensitive issue of Shari‘ah was not really addressed by SAMA [the Saudi Arabian Monetary Agency]”,⁴⁴ nor was it tackled by the Capital Markets Law of 2003.⁴⁵ These omissions are particularly ironic given the number of *shukūk* issuances and hedge funds as well as large Shari‘ah-compliant mutual funds businesses in Saudi Arabia.⁴⁶ Islamic banking business

⁴²See for example: Anwar Khalifa AI-Sadah, "Corporate Governance of Islamic Banks: Characteristics and Effects on Stakeholders and the Role of Islamic Banks Supervisors" (PhD thesis, University of Surrey, School of Management, 2007); Faris Mahmoud Abumouamer, "An Analysis of the Role and Function of the Shariah Control in Islamic Banks" (PhD thesis, University of Wales, College of Cardiff, 1989); Zulkifli Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK" (PhD thesis University of Durham, School of Government and International Affairs, 2011).

⁴³Rodney Wilson, "The Development of Islamic Finance in the GCC," *LSE Centre for the Study of Global Governance*, May 2009(2009) <http://www2.lse.ac.uk/government/research/resgroups/kuwait/documents/Wilson.pdf> accessed 10 November 2010

⁴⁴Ibid., P5,7.

⁴⁵Saudi Arabia, "Capital Market Law" Capital Market Authority (CMA), <http://www.cma.org.sa/En/AboutCMA/CMALaw/Documents/CAPITAL%20MARKET%20LAW-26-8-009.pdf>. accessed 25 September 2011

⁴⁶Wilson, "The Development of Islamic Finance in the GCC"; Zulkifli Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK," *Kyoto Bulletin of Islamic Area Studies on Islamic Finance* 3, no. 2 (2010).

accounts for 64% of the overall market share in Saudi Arabia.⁴⁷ The choice of the United Kingdom relates to its status as a secular country with a growing Islamic banking industry and a large Muslim population that has a vested interest in the Islamic banking system. London is the largest international hub for Islamic finance outside of Islamic countries.⁴⁸ It has the largest number of IIFS in Western Europe, with twelve Islamic banks in addition to ten main international banks that have established divisions to offer Islamic financial services.⁴⁹

Maintaining Financial Stability

Compliance with Shari‘ah law is one of the fundamental tenets of Islam, which requires Muslims to incorporate its principles into every aspect of their lives. Any financial services offered to the Muslims, therefore, must comply with Shari‘ah principles.⁵⁰ Parkinson suggests that the growth of Islamic finance will increase to such levels that it will be the standard in many Muslim countries; conventional banking might well become the exception,⁵¹ since clients of conventional finance can buy Islamic finance products, but not vice versa.⁵² Failure to ensure Shari‘ah compliance could pose a serious threat to the stability of the Islamic financial services industry,⁵³ as it may lead to a lack of confidence from clients that results in what

⁴⁷Khan and Bhatti, "Islamic Banking and Finance: On Its Way to Globalization," p714.

⁴⁸ The Islamic Bank of Britain was the first British Islamic bank to be licensed. HSBC, Lloyds TSB, Barclays Capital, and other conventional banks offer Islamic finance products for their clients. See Abu Umar Faruq Ahmad and Muhammad Fazlul Karim, "Legal and Regulatory Issues in Islamic Finance Industry: The Evidence from UK and Australia," *6th International Islamic Finance Conference* (2008) <http://www.kantakji.com/fiqh/Files/Markets/c35.pdf> accessed 10 November 2010.

⁴⁹U. K. Trade Investment, *The City: UK excellence in Islamic Finance*

(London: UK Trade & Investment, 2008), P2. See also, Rodney Wilson, *Islamic Finance in Europe* (Florence: European University Institute, 2007), p2; Abdul Karim Aldohni, *The Legal and Regulatory Aspects of Islamic Banking : a Comparative Look at The United Kingdom and Malaysia* (London: Routledge, 2011), p21.

⁵⁰Ayub, *Understanding Islamic Finance*, p475.

⁵¹Giles Parkinson, "Faith in The System," *Intheblack*, http://findarticles.com/p/articles/mi_qa5393/is_200708/ai_n21294575/ accessed 16 March 2011.

⁵²Ibid.

⁵³ See: Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p288.

might be called an “Islamic bank run”.⁵⁴ Unlike depositors in conventional banks, depositors in Islamic banks might withdraw their money not mainly out of fear of losing it, but out of concern about its usage for investment purposes that they may deem as non-Shari‘ah compliant, given that Shari‘ah compliance is one of the key motivations for dealing with an Islamic bank in the first place.⁵⁵ Jonathan Ercanbrack⁵⁶ points out this distinctive reputational risk of Islamic finance products and criticises the financial regulators in the UK for failing to mitigate that risk by regulating the religious aspect of these products, instead applying the same regulatory treatment to Islamic and conventional financial sectors.⁵⁷ According to a study conducted by Chapra and Ahmed, nearly 86% of depositors in Bahraini Islamic banks, in addition to 95% in Sudanese Islamic banks, would be prepared to withdraw their money if the banks were found not to be complying with Shari‘ah law.⁵⁸

Protecting Consumers

Consumer protection and effective financial systems are the key objectives of all financial regulators.⁵⁹ The absence of an effective and standardised framework which ensures Shari‘ah compliance could result in consumers discovering that they have

⁵⁴ This phrase was coined by Professor Dalvinder Singh.

⁵⁵ Abdul Karim Aldohni, "Islamic Banking Challenges Modern Corporate Governance: The Dilemma of The Shari'a Supervisory Board," *Company Lawyer* 29, no. 5 (2008).

⁵⁶ Jonathan Ercanbrack, "The Regulation of Islamic Finance in the United Kingdom," *Ecclesiastical Law Journal* 13, no. 1 (2011): p69-71.

⁵⁷ The HM tax arrangement for Islamic financial products suggests an awareness that the economic substance of these products does not differ from that of the conventional ones. H. M. Treasury, "The Development of Islamic Finance in the UK the Government's perspective," HM Treasury, http://webarchive.nationalarchives.gov.uk/20120306210332/http://www.hm-treasury.gov.uk/d/islamic_finance101208.pdf. accessed 10 May 2013.

⁵⁸ M. Umer Chapra and Habib Ahmed, *Corporate Governance in Islamic Financial Institutions* (Jeddah: Islamic Development Bank, 2002), p119; Assem Safieddine, "Islamic Financial Institutions and Corporate Governance: New Insights for Agency Theory," *Corporate Governance: An International Review* 17, no. 2 (2009): p146.

⁵⁹ See for example : United Kingdom, "Financial Services and Markets Act 2000 : Chapter 8," The National Archives, http://www.legislation.gov.uk/ukpga/2000/8/pdfs/ukpga_20000008_en.pdf. accessed 15 May 2013; "Financial Services Act 2012," The National Archives, http://www.legislation.gov.uk/ukpga/2012/21/pdfs/ukpga_20120021_en.pdf. accessed 17 May 2013

purchased a non-Shari‘ah-compliant product.⁶⁰ In 2009, Taqi Usmani, a leading figure in the field of Islamic finance, stated that “many structures presenting themselves as Islamic didn’t meet the definition of true Shari‘ah compliance”.⁶¹ Moreover, a study funded by the Dutch Central Bank suggests that Islamic financial consumers enjoy less protection than their counterparts in conventional finance.⁶²

Mitigating Legal Risk

Creative Shari‘ah compliance in the Islamic finance industry manifests itself in many ways which run the risk of legal challenge. This is especially the case when Islamic parties lack the capacity to sign a non-Shari‘ah-compliant contract. It is suggested that this can call into question the enforceability of the contract in both Muslim and secular countries. Concerns have also arisen over the legality of Islamic financial instruments and the uncertainty of law in relation to Shari‘ah.⁶³ In *Investment Dar v Blom Development Bank*,⁶⁴ for instance, a claimant who defaulted on a \$100 million *ṣukūk* argued in its defence that the contract in question was not Shari‘ah compliant, despite the fact that its own Shari‘ah board had approved it as such. On the other hand, Rider⁶⁵ argues that if an IIFS offered a Shari‘ah-compliant product that does not actually comply with Islamic law, it might be liable for breach of contract or misrepresentation. It could be also liable for mis-selling under various consumer protection laws and regulations.

⁶⁰See: Hamdan, "Non-Sharia Compliance Costs sSukuk Industry Billions"; Mahdi, "Most of Islamic Financial Products are not Islamic". ; Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p288.

⁶¹Shaheen Pasha, "Sharia Boards face Scrutiny amid Financial Crisis," Reuters, <http://www.reuters.com/article/2010/03/11/islamic-scholars-idUSLDE62A0J420100311>. accessed 10 December 2010.

⁶²Bastiaan Verhoef, Somia Azahaf , and Bijkerk Werner, *Islamic Finance and Supervision: an Exploratory Analysis* (Amsterdam: De Nederlandsche Bank, Eurosysteem, 2008), p32.

⁶³Djojosedjito, "Mitigating Legal Risk in Islamic Banking Operations."; Sole, "Introducing Islamic Banks into Conventional Banking Systems". p4.

⁶⁴*Investment Dar Co KSCC v Blom Developments Bank Sal*, [2009] EWHC 3545 (Ch)(2009).

⁶⁵Barry Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," in *Islamic Finance: Law and Practice*, ed. Craig Nethercott and David Eisenberg (Oxford: Oxford University Press, 2012), p136.

Boosting Economic Efficiency

Creative Shari'ah compliance in the Islamic finance industry presents the additional problem of increasing economic costs. The process of restructuring conventional products to meet Shari'ah requirements to the letter necessitates a network of complex contracts. These might involve establishing many special-purpose vehicles which ultimately increase the legal cost of the transaction, although they neither present economic benefits nor add value for clients other than the deceptive appearance of Shari'ah compliance.⁶⁶As Nikan Firoozye notes,⁶⁷ questioning the Shari'ah authenticity of a product offered as Shari'ah compliant,

The Shari'ah compliant option was altogether worse than its conventional counterpart. For one thing, the fee was likely to be larger than an option premium, including portions to reimburse bankers, structures, Shari'ah scholars, salesmen and shareholders for their time and capital. All this for merely repackaging a forex call or put option and calling it a *wa'd* or promissory note.

Scope of the Study

The primary focus of this research is the issue of creative Shari'ah compliance in the Islamic finance industry from a regulatory perspective. This thesis does not attempt to discuss the economic or religious justifications of Islamic finance, since these issues are well recognised in the literature.⁶⁸

In addition, the discussion of this study is limited to the discourse of *sunni* Islamic schools of thought, starting with the four major *sunni madhhab* (schools of thought), Ḥanafī, Shāfi'ī, Mālikī, and Ḥanbalī, which have the greatest impact on contemporary Islamic finance. Nonetheless, it occasionally addresses the position of other schools which have less impact over the industry but could play an active role in the future.

⁶⁶El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p6,21-23; Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p238.

⁶⁷Firoozye, "Wa'd and the completeness of Islamic markets".

⁶⁸ Refer to survey provided by Siddiqi, "Banking and Finance in Theory and Practice: A Survey of the State of the Art," p1.

Although this thesis makes special reference to Saudi Arabia and the UK, due to the fluid and integrated nature of Islamic finance, the research refers to other jurisdictions when necessary.

Methodology

This research is primarily library based. It analyses classical and contemporary *fiqh* (Islamic jurisprudence) literature in addition to relevant legislation, official reports, textbooks, articles, and online databases both in Arabic and in English. The thesis mainly takes a non-doctrinal approach,⁶⁹ since investigating the issue of creative Shari‘ah compliance in the Islamic finance industry is, in a way, examining the gap between the “law in books” and “law in action”. This research acknowledges the positions of regulators in Islamic and secular countries and suggests reforms to the current framework which can benefit the stakeholders and protect the consumers of Shari‘ah-compliant products. However, as Dobinson and Johns note,⁷⁰ an extensive study tends to include a doctrinal part where the researcher attempts to determine the existing law in a specific area before highlighting its deficiency and suggesting alternatives. Such is the case here.

In dealing with the classical and contemporary Islamic jurisprudence literature, the thesis combines the approach of “Scholastic Neo-traditionalism”⁷¹ with a “*maqāṣid* [objective]-based” approach.⁷² The former is not restricted to one Islamic school of thought. It studies how each school of thought concluded its view and

⁶⁹Ashish Kumar Singhal and Ikramuddin Malik, "Doctrinal and socio-legal methods of research: merits and demerits," *Educational Research Journal* 2, no. 7 (2012): p253.

⁷⁰Ian Dobinson and Francis Johns, "Qualitative Legal Research," in *Research Methods for Law*, ed. Wing McConville Mike Hong Chui (Edinburgh: Edinburgh Univ. Press, 2007), p20.

⁷¹Jasser Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach* (London: International Institute of Islamic Thought, 2008), p164.

⁷²*Ibid.*, p176; Halim Rane, "Issues in Legal Thought," in *Islam and Contemporary Civilisation : Evolving ideas, Transforming Relations* (Melbourne, Vic.: Melbourne University Publishing, 2010), p93

whether that view is supported by the primary sources of Shari‘ah.⁷³ It is currently, as noted by Auda,⁷⁴ the most widely applied approach to Islamic legal research. The latter places particular importance on the *maṣlahah* (public interest), the objectives of the legal texts, and the intent of the lawgiver rather than merely on specific words or verses.⁷⁵ The objective-based approach is highly relevant to the topic of this thesis, since the practises of creative Shari‘ah compliance flout the objective which Islamic law tries to achieve.

Structure of the Thesis

The thesis consists of this introduction, seven chapters, and a conclusion. Chapter one, “An Overview of Shari‘ah“, provides a short introduction to Shari‘ah (Islamic law) and the key features of Islamic finance, familiarising the reader with the basic concepts of Islamic law before presenting the main topic of this thesis. Chapter two, “The Form Versus Substance Debate and the Roots of Creative Shari‘ah Compliance in Islamic Finance: Why Reinvent the Wheel?” moves into the thesis’s primary area of exploration, examining whether creative Shari‘ah compliance is a phenomenon new to Islamic law. It investigates the positions of the various schools of thought on issues related to “substance” and “form” in Islamic finance, and it surveys whether classical Islamic jurisprudence justifies using *ḥīlah* (a legal ruse) to practise creative Shari‘ah compliance.

Chapter three, “*Tawarruq* as a Case Study of Creative Shari‘ah Compliance”, illustrates creative Shari‘ah compliance in the Islamic finance industry by examining *tawarruq*, one of the most common structures used by IIFS to offer Shari‘ah-

⁷³ See: Mahdi Zahraa, "Unique Islamic Law Methodology and the Validity of Modern Legal and Social Science Research Methods for Islamic Research," *Arab law quarterly Arab law quarterly* 18, no. 3-4 (2003): p223.

⁷⁴ Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p164.

⁷⁵ *Ibid.*, p172.

compliant products and services. The next chapter, “Standardisation of *Fatwas* to Reduce Creative Shari‘ah Compliance”, examines the inconsistency in the *fatwas* issued by Shari‘ah supervisory boards (SSBs) that reside in various financial institutions as a key factor contributing to the issue of creative Shari‘ah compliance. It evaluates the suitability of standardisation as a mechanism to reduce conflict in the opinions of Shari‘ah scholars concerning the permissibility of financial products, addressing the arguments for and against standardisation and investigating the causes of juristic differences. This chapter traces the legal theories offered in classical Islamic jurisprudence to deal with this issue, then suggests potential remedies and highlights the limitations of implementing them in Islamic and secular countries.

Chapter five, “The Impact of Shari‘ah Governance Practises on Shari‘ah Compliance in Contemporary Islamic Finance”, explores definitions of SSBs in Islamic finance literature as well as highlighting the importance of SSBs to IIFS structure. It then examines the impact of regulatory issues surrounding SSBs on Shari‘ah compliance in the contemporary Islamic finance industry, identifying seven challenges as major factors in reducing the level of Shari‘ah compliance in IIFS. These are the SSBs’ conflicting responsibilities, unclear functions and legal status, and lack of independence, accountability, and transparency, combined with the poor training and the inadequate qualifications of SSB members.

Chapters six and seven draw on the findings of earlier chapters to propose remedies for creative Shari‘ah compliance. Chapter six, “Public Mechanisms to Remedy Creative Shari‘ah Compliance”, suggests two public mechanisms that involve a national body in remedying the issue of creative Shari‘ah compliance: establishing central Shari‘ah supervisory boards (CSSBs) and enforcing compulsory disclosure. It addresses the limitations of CSSBs, considering the central Shari‘ah boards in Sudan and Malaysia, and examines regulators’ approaches in the UK and the KSA towards Shari‘ah governance and CSSBs. The following chapter, “Private Mechanisms to Remedy Creative Shari‘ah Compliance”, suggests six mechanisms to remedy creative Shari‘ah compliance which can be employed by private actors in the industry without government involvement. Four of these mechanisms are external: adopting a Shari‘ah compliance rating, Shari‘ah indices, private Shari‘ah auditing, and international standards related to enhancing Shari‘ah compliance. The remaining two mechanisms are internal: a whistle-blowing policy for serious Shari‘ah-compliance violations and a clause in IIFS articles of association that characterises the IIFS as an entity that fully complies with Shari‘ah ruling. These remedies are particularly useful when an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari‘ah governance.

Finally, the conclusion summarizes the study’s findings, drawing on them to offer suggestions and recommendations to reduce the practise of creative Shari‘ah compliance in the industry and to enhance general Shari‘ah compliance in IIFS.

Chapter One:

An Overview of Shari‘ah

1.1. Introduction

This chapter provides a short introduction to Shari‘ah (Islamic law) and the key features of Islamic finance, familiarising the reader with the basic concepts of the law before reaching the main topic of this thesis. Since the scope of this research is limited, and these issues are well recognised in the literature, the discussion is confined to a general overview of the subject.

This chapter consists of eight parts, including this introduction. Part 1.2 presents an overview of Shari‘ah and its origins, Part 1.3 provides a short history of the schools of Islamic law, Part 1.4 gives a necessary introduction to Islamic legal rulings, Part 1.5 addresses the main features of Islamic finance, Part 1.6 outlines the key Shari‘ah-compliant financial instruments, Part 1.7 highlights the objectives of Islamic law, and finally, Part 1.8 concludes the chapter.

1.2. Overview of Shari‘ah and Its Foundation

Shari‘ah is an Arabic word which means literally “the path” or “the way”.⁷⁶ In a religious context, it refers to the path that Allah (God) has formed for human beings to follow. Shari‘ah covers the spiritual as well as the daily practises of Muslim life, as Islam assumes no division between the secular and the religious. The complete power of God is a fundamental faith of the Islam. Hence, Allah, according to Islam, “is the source of authority and the sole sovereign lawgiver”.⁷⁷

⁷⁶ S. Kunhibava and Rachagan S., "Shariah and Law in Relation to Islamic Banking and Finance," *Banking and Finance Law Review* 26, no. 3 (2011): p544; Charles P Trumbull, "Islamic Arbitration: A New Path for Interpreting Islamic Legal Contracts " *Vand. L. Rev* 59, no. 2 (2006): p626. An earlier version of this section was published as: Ahmad Alkhamees, "International Arbitration and Shari'a Law: Context, Scope, and Intersections," *Journal of International Arbitration* 28, no. 3 (2011).

⁷⁷ Faisal Kutty, "The Shari'a Factor in International Commercial Arbitration," *Loyola of Los Angeles international & comparative law review Loyola of Los Angeles International & Comparative Law Review* 28, no. 2 (2006): p578.

However, a distinction should be drawn between Shari‘ah and Islamic jurisprudence, commonly called “*fiqh*”, because some non-Muslim researchers tend to equate these terms.⁷⁸ Islamic jurisprudence is a subset of Shari‘ah, composing a single area of the broader concept. Shari‘ah serves as the basis of all principles formed and expanded under *fiqh*, whereas the term “Islamic jurisprudence” generally refers to scholarly comprehension and findings derived from the primary and secondary sources of Shari‘ah.⁷⁹

The main sources of Islamic law are the Quran⁸⁰ and the *sunnah*. The expression *sunnah* means the accumulation of the teachings of Prophet Muhammad, which includes his sayings, actions, decisions, and implicit approbation or disapproval of things.⁸¹ The secondary sources include *ijma* and *qiyas*. *Ijma* refers to the uncontested approval of qualified scholars on a certain matter of Islamic jurisprudence. *Qiyas* describes a methodical process of analogical reasoning that is applied when one considers an issue not explicitly treated in the primary sources of Shari‘ah. This procedure allows one to get from an identified injunction to a new injunction that applies Shari‘ah opinion to the issue in question.⁸² Some schools of thought recognise additional secondary sources for determining the Shari‘ah position on certain issues.⁸³ These include *urf*, the Arabic for “custom”, *maslahah mursalah* (public interest), and

⁷⁸ See: Abdulrahman Baamir and Ilias Bantekas, "Saudi Law as Lex Arbitri: Evaluation of Saudi Arbitration Law and Judicial Practice," *Arbitration International* 25, no. 2 (2009): p262.

⁷⁹ See: Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p57.

⁸⁰ “Quran” is an Arabic word which literally means “recitation”. The Quran is the holy book which Muslims believe was revealed from Allah (God) to the Prophet Muhammad. It is considered to be the highest religious text in Islam. See: "Quran," Oxford University Press, <http://www.oxfordislamicstudies.com/opr/t125/e1945>. accessed 04/12/2010

⁸¹ Kutty, "The Shari'a Factor in International Commercial Arbitration," p585. Trumbull, "Islamic Arbitration: A New Path for Interpreting Islamic Legal Contracts " p626-27. Mohammad Hashim Kamali, *Principles of Islamic Jurisprudence*, Third ed. (Cambridge, UK: Islamic Texts Society, 2003), p58.

⁸² *Principles of Islamic Jurisprudence*, p264.

⁸³ *Ibid.*, p306 and the following chapters.

*sadd al-dhariā'ī*⁸⁴ (precautionary legal prohibition), which entitle the blocking of actions that could lead to unlawful ends.⁸⁵

1.3. Schools of Thought

Although the main principles of Shari'ah and the essential doctrines of Islamic jurisprudence are identical, Islamic scholars have always debated the proper understanding of Shari'ah commands regarding the secondary issues, along with whether a certain rule can be applied in a particular situation.⁸⁶ This debate has resulted in the formation of many different *sunnī* schools of thought, or *madhabs*, as they are known in Arabic. These can be categorised into two general schools of thought: the school of *ahl al-ra'y*⁸⁷ (literally “the people of good sense”) in Iraq and the school of *ahl al-ḥadīth*⁸⁸ (the traditionalists) in Medina. The former generally includes those in favour of using independent legal arguments to conclude a Shari'ah ruling. The latter includes those who endeavour to base the law on the traditions of the Prophet and his companions. According to their view, it is illegitimate to favour or solely rely on unrestricted human reasoning, especially when it conflicts with an authentic *ḥadīth* (tradition).

Several *sunnī* schools have ramified from these two major schools of thought. Of these, however, only four major schools remain in the Islamic world today. This thesis primarily investigates the position of these schools of thought, since they have a great

⁸⁴ Literally “the blocking of means”; the blocking of actions that could lead to unlawful ends. See: *ibid.*, p397.

⁸⁵ See: ‘AbdAllāh Ibn Bayyah, *Sadd al-Dhari'ah wa Taṭṭbīqātuh fī Majāl al-Mu'āmalāt* (Islamic Development Bank, 1997), p48; Mir Siadat Ali Khan, "The Mohammedan Laws against Usury and How They Are Evaded," *Journal of Comparative Legislation and International Law* 11, no. 4 (1929): p240; Aḥmad ibn ‘Abd al-Ḥalīm Ibn Taymiyah, *al-Qawā'id al-Nawrānīh al-Fiqhiyah*, ed. Muḥammad Ḥāmid al-Faqī (Maktabah al-Sunnah al-Muḥammadiyyh, 1951), p119.

⁸⁶ *Ibid.*

⁸⁷ Peter C Hennigan, "Ahl al-ra'y," in *Encyclopaedia of Islam* (Brill, 2012) <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-3/ahl-al-ray-COM_22177> accessed 1 April 2012.

⁸⁸ See: Joseph Schacht, "Ahl al-Ḥadīth," *ibid.* <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/ahl-al-hadith-SIM_0379>

impact on contemporary Islamic finance.⁸⁹ These schools are the Ḥanafī School, named after its founder, the scholar Abū Ḥanīfah (d.150 AH/767 CE); the Mālikī School, named after its founder, Mālik Ibn Anas (d.179/795); the Shāfi‘ī School, named after the scholar Al-Shāfi‘ī (d.204/820); and finally the Ḥanbalī School, named after the scholar Aḥmad Ibn Ḥanbal (d. 241/855). Nevertheless, as Shari‘ah scholars are not considered infallible in Islam, all of the scholars’ *fatwas* concerning the secondary issues are regarded as equally applicable.

1.4. Islamic Legal Ruling

Unlike other legal systems in which immoral action is not necessarily illegal, in Islam it is very difficult to separate the two, as Shari‘ah law acts as the judge of what is legal in addition to what is good and evil.⁹⁰ Immoral actions can have a consequence in this world and the hereafter. For example, practicing usury not only is a sin, but also can result in the usurious contract being deemed *fāsīd* (void). The immorality of certain actions may sometimes be hidden (e.g., bad faith), causing the judge to consider those actions *ṣaḥīḥ qaḍā’an* (valid). Nonetheless, a person can be held accountable for such immoral action in the hereafter. The rest of this section further describes this framework.

Understanding these two notions within the Islamic legal ruling is necessary to appreciate the arguments in chapter two. The legal ruling of Shari‘ah (*al-ḥukm al-shar‘ī*) is divided into two categories: *al-ḥukm al-taklīfī* (defining law) and *al-ḥukm al-waḍ‘ī* (declaratory rulings or correlative law).⁹¹ These apply to human actions

⁸⁹ Occasionally, the thesis might explore the position of other schools of thought where it is relevant (e.g., where their views are cited in classical and contemporary literature on comparative jurisprudence)

⁹⁰ Frank E. Vogel and Samuel L. Hayes, *Islamic Law and Finance: Religion, Risk, and Return* (The Hague: Kluwer Law Internat., 1998), p41.

⁹¹ Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p137-40; Kamali, *Principles of Islamic Jurisprudence*, p413.

which, in Shari‘ah, generally have two dimensions: hidden and manifest.⁹² *Al-ḥukm al-taklīfī* is concerned with the inward hidden dimension and the accountability of a person in the hereafter, while *al-ḥukm al-waḍ‘ī* has more to do with the outward manifest dimension and individuals’ rights and relations in this world.⁹³ For example, if two people connive to testify falsely against another person, their agreement is prohibited from the *al-ḥukm al-taklīfī* perspective, but the testimony itself before a judge is valid from the *al-ḥukm al-waḍ‘ī* perspective, assuming there is no evidence of their false testimony.⁹⁴ Another example is the action of selling property to avoid payment of *zakāh* (obligatory charity tax). The hidden side of this action is subject to the classification of the defining law, which prohibits the transaction as it aims to avoid obligation.⁹⁵ The manifest side is subject to classification of the correlative law, which deems the transaction valid since it appears to be a legal exchange.⁹⁶

Al-ḥukm al-taklīfī defines the scope of a person’s liberty of action.⁹⁷ It can embody a demand that the *mukallaḥ* (religiously accountable person) take an action or refrain from one, or it can allow him to choose between the two. *Al-ḥukm al-waḍ‘ī* plays a descriptive role in relation to *al-ḥukm al-taklīfī*. It is a communication from the lawgiver (Allah) which decrees something into *sabab* (a cause), a *sharṭ*

⁹² See: ‘AbdAllāh Marzūq al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī* (Namaa for Research and Studies Centre, 2012), p320; Aḥmad ibn ‘Abd al-Ḥalīm Ibn Taymiyah, *al-Fatāwā al-Kubrā*, ed. Muḥammad ‘atā and ‘abd al-Qādir ‘atā, vol. 6 (Dār al-Kutub al-‘ilmiyyah, 1987), p190.

⁹³ See: *al-Fatāwā al-Kubrā*, 6, p190; al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī*, p320; Wael B. Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh* (Cambridge, UK: Cambridge University Press, 1997), p41.

⁹⁴ Aḥmad ibn ‘Abd al-Ḥalīm Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, ed. Ḥamdī ‘Abd al-Majīd al-Salaḥī (al-Maktab al-Islāmī, 1988), p309; Muḥammad bn Abī Bakr Ibn al-Qayyim, *I’lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, ed. Ṭah ‘Abd al-Ra’uf Sa’d, vol. 3 (Dār al-Jīl, 1973), p281.

⁹⁵ For the prohibition of avoiding *zakāh* in this case see: *I’lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p208; Aḥmad ‘Umar al-Khaṣṣāf, *Kitāb al-Ḥiyal* (Maṭba‘ah al-Qāhirah, 1896), p6; Ya‘qūb Ibrāhīm Abū Yūsuf, *Kitāb al-Kharāj* (Dār al-Ma‘rifah, 1979), p82.

⁹⁶ See generally: al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī*, p210.

⁹⁷ Kamali, *Principles of Islamic Jurisprudence*, p413.

(condition), or a *māni*⁹⁸ (hindrance), or declares an action to be *ṣaḥiḥ* (valid) or *fāsid* (void).⁹⁸

Al-ḥukm al-taklīfī subdivides actions into five classes: *wājib* (obligatory), *mastahab* (recommended), *muḥarram* (prohibited), *makrūh* (discouraged), and *mubāḥ* (neutral or indifferent). Actions classified as prohibited or obligatory fall under the umbrella of law, since law by its nature imposes obligation and prohibits certain actions, and it usually rewards those who follow it and punishes those who defy it. However, recommended (*mastahab*) and discouraged (*makrūh*) acts cannot be considered part of a legal framework, at least directly, because complying with the recommendation attracts a reward, but failure to comply carries no punishment. Nevertheless, both kinds of classifications are integral components of the Islamic legal system,⁹⁹ as Shari‘ah pays similar attention to recommended and disapproved acts as to prescribed and prohibited acts. Likewise, the neutral classification (*mubāḥ*) cannot be subsumed under the heading of law, although classical scholars have debated whether arguments exist that would justify its inclusion under the category of defining rulings.¹⁰⁰ The neutral level is not only out the realm of obligatory and prohibited classification, but also outside the recommended and disapproved classes. It falls outside the two categories as it attracts neither reward nor punishment.¹⁰¹

⁹⁸ See for example: Ibrāhīm Mūsā al-Shātibī, *al-Muwāfaqāt*, ed. Mashhūr Ḥasan Salmān, vol. 1 (Dār Ibn ‘Affān, 1997), p297; Kamali, *Principles of Islamic Jurisprudence*, p413. Muḥammad ‘Alī al-Āmidī, *al-Iḥkām fī Uṣūl al-Aḥkām*, ed. Sayyid al-Jamīlī, vol. 1 (Dār al-Kitāb al-‘Arabī, 1984), p137. The majority of schools uphold that there are no different levels of invalidity. However, the Ḥanafī School differentiates between two degrees of invalidity: *bāṭil* (void or null) and *fāsid*. A contract is deemed *bāṭil* if it lacks an essential element; it is considered nonexistent and establishes no legal effect. However, if the contract only lacks a non-essential element such as a condition, it is called *fāsid*. This is a degree between valid and void where the contract produces some of its legal effects. For example, a *fāsid* transaction establishes the ownership of the purchaser, but it does not entitle him to the usufruct *intifā’*.

⁹⁹ Bernard Weiss, *The Spirit of Islamic Law* (Athens, University of Georgia Press, 1998), p19-22. Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*, p40-41.

¹⁰⁰ al-Āmidī, *al-Iḥkām fī Uṣūl al-Aḥkām*, 1, p170.

¹⁰¹ Weiss, *The Spirit of Islamic Law*, p20.

With regard to *al-ḥukm al-waḍ'ī*, this thesis is concerned with the classification of an action as valid or void. The notion of validity (*al-ṣiḥḥah*) as a part of declaratory rulings is based on whether an action has been performed correctly, resulting in an obligation being fulfilled or a transaction taking effect.¹⁰² If, for example, a deal is concluded in way that does not comply with Shari'ah requirements for a contract of sale, it will not create the binding legal effect of transferring ownership.

1.5. Main Features of Islamic Finance

In Shari'ah, the starting assumption for all contracts and conditions is permissibility.¹⁰³ Verse 2:275 of the Quran reads, "Allah has permitted trade and has forbidden interest".¹⁰⁴ However, for a contract to be Shari'ah compliant, it must avoid certain restrictions, or be free of a number of prohibitions. Below is a summary of the three main factors which can render a contract non-Shari'ah compliant.

1.5.1. Ribā

The prohibition of *ribā* is perhaps the most distinctive feature of Islamic finance.¹⁰⁵ The Arabic word *ribā* literally means an increase or growth. *Ribā* tends to be translated in English as "usury" or "interest", although it has a wider meaning in Shari'ah.¹⁰⁶ However, this thesis uses these translations interchangeably. A transaction will be deemed *ribawī* (usurious) if it has one or both of the following elements:

¹⁰² See: *ibid.*, p21; Kamali, *Principles of Islamic Jurisprudence*, p438.

¹⁰³ Wahbah al-Zuhayli, *Financial Transactions in Islamic Jurisprudence*, trans. El-Gamal Mahmoud A. and Eissa Muhammad S., vol. 1 (Damascus, Syria: Dar al-Fikr, 2007), p7.

¹⁰⁴ Saheeh International, *Translation Of The Meanings Of The Glorious Quran* (al-Muntada al-Islami, 2004).

¹⁰⁵ El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p49.

¹⁰⁶ Tarek El Diwany, ed. *Islamic Banking and Finance : What it is and What it could be* (Bolton: 1st Ethical Charitable Trust, 2010), p99.

1. “An excess (*al-faḍal*) in the amount of one countervalue over the other in barter transactions of specific commodities”.¹⁰⁷
2. “A delay (*al-nsa’*) in the settlement of one or both countervalues”.¹⁰⁸

Accordingly, two types of *ribā* are recognised: *ribā al-qurūd* (the usury of loans) and *ribā al-buyū’* (the usury of trade).¹⁰⁹ An example of the former is lending one ounce of gold now and collecting two ounces of gold in return two weeks later. An example of the latter is exchanging one kilogram of good-quality dates for three kilograms grams of poor-quality dates.

One thing to bear in mind is that unlike other sins, *ribā* is strictly prohibited in Islam.¹¹⁰ This prohibition can be drawn from several verses of the Quran and a number of *hadīth*. For example, verses 2:278–279 read:

O you who have believed, fear Allah and give up what remains [due to you] of interest, if you should be believers. And if you do not, then be informed of a war [against you] from Allah and His Messenger. But if you repent, you may have your principal—[thus] you do no wrong, nor are you wronged.¹¹¹

Besides, a contract will be invalidated if it includes a *ribā* clause.¹¹² The lender and the borrower in addition to the writer and the witness of a usury contract are all equally guilty of the wrongdoing, as stated in the following *hadīth*:

Jabir said that Allah's Messenger cursed the acceptor of interest and its payer, and one who records it, and the two witnesses, and he said: They are all equal.¹¹³

¹⁰⁷ These commodities are mentioned in a *hadīth* which has been narrated on the authority of Abu Sa’id al-Khudri. In it, the prophet said, “Gold is to be paid for by gold, silver by silver, wheat by wheat, barley by barley, dates by dates, salt by salt, like by like, payment being made hand to hand. He who made an addition to it, or asked for an addition, in fact dealt in usury. The receiver and the giver are equally guilty.” Shariah scholars—with the exception of the Zāhirī School—use analogy to extend the ruling to other items. See: *ibid*.

¹⁰⁸ *Ibid*.

¹⁰⁹ See: al-Zuḥaylī, *Financial Transactions in Islamic Jurisprudence*, 1, p311.

¹¹⁰ Ayub, *Understanding Islamic Finance*, p44.

¹¹¹ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

¹¹² al-Zuḥaylī, *Financial Transactions in Islamic Jurisprudence*, 1, p311.

¹¹³ Muslim ibn al-Hajjaj al-Naysaburi, "Sahih Muslim," Sunnah.com, <http://sunnah.com/muslim/22/132>. accessed 10 January 2014; Book 22, *Hadīth* 132.

Although Shari‘ah scholars unanimously agree on the prohibition of *ribā*, they dispute its scope and some of its rules which have been discussed extensively in Islamic jurisprudence literature.¹¹⁴ The details of such discussion are beyond the limit of this thesis; the important point here is that there is a general agreement on the prohibition of interest-bearing loans.¹¹⁵

1.5.1.1. Time Value of Money

Shari‘ah’s prohibition on usury does not mean that it entirely dismissed the notion of the time value of money.¹¹⁶ For instance, if a seller opts to sell his property on a deferred basis, he is permitted to charge a higher price than what he usually charges on a cash basis.¹¹⁷ Moreover, in an investment, the supplier of capital can gain a return for his capital in a profit- and loss-sharing agreement with the investor. Yet the return is not guaranteed, because in contrast to conventional finance, Shari‘ah does not recognise money as a commodity but as a medium of exchange.¹¹⁸ The capital provided to the investor is thus subject to the same uncertainties faced by other partners in the enterprise.

1.5.2. Gharar

Another important principle of Islamic finance is the prohibition of *gharar*, which tends to be translated as risk or uncertainty.¹¹⁹ It is difficult to provide a

¹¹⁴ See: al-Zuhaylī, *Financial Transactions in Islamic Jurisprudence*, 1, p313; Tarek El Diwany, *The Problem With Interest*, 3d ed. (London: Kreatoc, 2003), p157; El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p49; Ayub, *Understanding Islamic Finance*, p44; El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p99; Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p71.

¹¹⁵ El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p50.

¹¹⁶ Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p2.

¹¹⁷ al-Maṣrī argues that Shari‘ah recognises the time value of money on loans by promising reward in the hereafter for charitable loans. See: Rafiq Ūnis al-Maṣrī and Muḥammad riyāḍ al-Abrash, *al-Ribā wa al-Fā'idh : dirāsah aqtiṣādiyyah muqārīnah* (Damascus: Dār al-Fikir, 2001), p24.

¹¹⁸ Shaheen Sardar Ali and Musa Usman Abubakar, "Part 1: Islamic Finance Techniques: the Sunni schools' differing approaches," *Butterworths Journal Of International Banking & Financial Law* 25, no. 5 (2010).

¹¹⁹ See: Muhammad Akram Khan, *Islamic Economics and Finance : a Glossary* (London; New York: Routledge, 2003), p66. Ayub, *Understanding Islamic Finance*, p57.

comprehensive definition for *gharar*,¹²⁰ since the Arabic root of the word can be associated with various notions such as fraud, deception, danger, fallaciousness, and uncertainty.¹²¹ Al-Zarqa' defines *gharar* as “the sale of probable items whose existence or characteristics are not certain, due to the risky nature which makes the trade similar to gambling”.¹²² Al-Suwaylim attempts to quantitatively define a *gharar* transaction by equating it to “a zero-sum game with uncertain payoffs”.¹²³ *Gharar* can occur when uncertainty surrounds the existence, possession, availability, price, and deliverability of the object of a contract. It also can occur where the terms of a contract are uncertain (e.g., making a sale contingent on a future event such as “snow on day X”). A classic example of a *gharar* transaction is selling a fish in the sea. Importantly, minor *gharar* is forgiven; only major *gharar* (excessive risk or uncertainty) will invalidate a contract.¹²⁴ By forbidding *gharar*, Shari‘ah aims to reduce the chances of exploitation and dispute in society.¹²⁵ In the financial context, the principle of avoiding *gharar* is relevant to determining the Shari‘ah view on the insurance market and financial derivatives.¹²⁶

1.5.3. Maisir and Qim’ar

Another important principle in Islamic finance is the prohibition of *maisir* and *qim’ar*.¹²⁷ The former can be translated as “gambling”, where wealth can be acquired by chance or easily without compensating for it or incurring liability against it. The

¹²⁰ See generally: Sami Al-Suwailem, "Towards An Objective Measure of Gharar in Exchange," *Islamic Economic Studies* 7, no. 1 (2000): p61. al-Saddiq Muhammad al-Amin al-Darir, *Al-Gharar in contracts and its effects on contemporary transactions* (Jiddah: Islamic Research and Training Institute, 1997); Abdurrahim al-Saati, "The Permissible Gharar (Risk) in Classical Islamic Jurisprudence " *Islamic Economics* 16, no. 2 (2003).

¹²¹ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p114.

¹²² Mahmoud Amin El-Gamal, *A Basic Guide to Contemporary Islamic Banking and Finance* (Houston, TX: Rice University, 2000), p6.

¹²³ Al-Suwailem, "Towards An Objective Measure of Gharar in Exchange," p86.

¹²⁴ al-Darir, *Al-Gharar in contracts and its effects on contemporary transactions*, p44; al-Saati, "The Permissible Gharar (Risk) in Classical Islamic Jurisprudence ".

¹²⁵ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p114.

¹²⁶ El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p61.

¹²⁷ Ayub, *Understanding Islamic Finance*, p62.

latter can be translated as “a game of chance”, in which two competitive parties take on a risk of loss, and the gain for one is the loss of the other.¹²⁸ On the subject of *maisir*, verse 5:90 of the Quran reads:

O you who have believed, indeed, intoxicants, gambling, [sacrificing on] stone alters [to other than Allah], and divining arrows are but defilement from the work of Satan, so avoid it that you may be successful.¹²⁹

In the same vein, verse 2:219 reads:

They ask you about wine and gambling. Say, “In them is great sin and [yet, some] benefit for people. But their sin is greater than their benefit”.¹³⁰

According to Ayub,¹³¹ *qim'ar* is an important subset of *maisir* (gambling), which itself is a form of *gharar* since gamblers are uncertain about the outcome of their gamble. The principle of avoiding *maisir* and *qim'ar* is highly relevant to the Shari'ah view on investing in companies with gambling as a primary source of income. It is also relevant to assessing the Shari'ah compliance of public and private sector schemes where resources are mobilised on the basis of lotteries and draws.¹³²

1.6. Shari'ah-Compliant Financial Instruments

Authors have taken different approaches when presenting Shari'ah-compliant contracts.¹³³ This thesis categorises Shari'ah-compliant financial instruments into two groups: equity-type contracts and debt-financing contracts. Examples of relevant instruments from each group are provided below.

¹²⁸ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p114.

¹²⁹ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

¹³⁰ Ibid.

¹³¹ Ayub, *Understanding Islamic Finance*, p62; Kunhibava and S., "Shariah and Law in Relation to Islamic Banking and Finance," p549.

¹³² Ayub, *Understanding Islamic Finance*, p62.

¹³³ Compare the following: al-Zuhayli, *Financial Transactions in Islamic Jurisprudence*, 1, p 3; Ayub, *Understanding Islamic Finance*, p105; El-Gamal, *A Basic Guide to Contemporary Islamic Banking and Finance*, P vi; *Islamic Finance : Law, Economics, and Practice*, p VIII; Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p129; El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p91.

1.6.1. Equity-Type Contracts

Instruments of equity-type contracts are based on the principle of profit- and loss-sharing (PLS) which is the backbone of the Islamic financial system.¹³⁴ Although this type of contract is the most compliant with the objectives of Islamic law,¹³⁵ it is the least practised form of Islamic finance.¹³⁶ This section discusses two forms of this type of contract, *mushārah* and *mudaraba*.

Mushārah (partnership)¹³⁷ is a PLS agreement between two or more parties in which all the partners provide capital and have the right to manage the business venture. The ratio of profit distribution must be pre-agreed, but it can be negotiated between the parties and does not necessarily need to reflect the percentage of capital contribution.¹³⁸ However, unlike in conventional finance, where parties are free to negotiate the ratio of loss distributions, in *mushārah* the loss is shared between all partners in ratio to their capital participation. In addition, each partner is jointly liable to a third party for the actions of other partners (e.g., negligence).¹³⁹

Mudaraba (silent partnership or trustee profit-sharing)¹⁴⁰ is a partnership agreement in which one party known as *rabb ul-mal* (investor or silent partner) provides capital to another party known as *mudarib* (entrepreneur or trustee of the venture) to invest in a business venture. Funds and labour are equally recognised methods of creating wealth. Therefore, both parties generally share the profit of the

¹³⁴ See: Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari`ah in Islamic Banking and Finance," p4-5.

¹³⁵ Usmani, *An Introduction to Islamic Finance*, p12; Abd Jabbar, "Sharia-Compliant Financial Instruments: Principles and Practice," p179.

¹³⁶ See: Samad, Gardner, and Cook, "Islamic Banking and Finance in Theory and Practice: The Experience of Malaysia and Bahrain," p83; Sechafia et al., "What Drives An Ideal Islamic Finance? A Maqasid Compliance Approach," p11-13; Eddy Yusof, Kashoogie, and Anwar Kamal, "Islamic Finance: Debt versus Equity Financing in the Light of Maqasid al-Shari'ah." p5-6.

¹³⁷ Usmani, *An Introduction to Islamic Finance*, p19.

¹³⁸ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p158.

¹³⁹ Abd Jabbar, "Sharia-Compliant Financial Instruments: Principles and Practice," p176. Usmani, *An Introduction to Islamic Finance*, p31.

¹⁴⁰ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p162.

venture.¹⁴¹ The ratio of profit distribution must be pre-agreed and can be negotiated between the parties. Unlike in conventional finance, the capital provider is guaranteed a definite return or a fixed annual payment. In the event of a loss, the investor loses his capital, while the trustee of the venture loses his time and effort in running the business.¹⁴² In case the trustee of the venture takes action that does not comply with the conditions and limitations agreed upon with the investor, his action is deemed *ultra vires* and he is liable for any loss or damage resulting from his action.¹⁴³

The above-mentioned accounts of *mushārah* and *mudaraba* only cover the basic notion of the two instruments. Shari‘ah scholars’ discussion on issues related to the two forms, as well as challenges in applying these instruments in the modern financial system, is well researched in the literature.¹⁴⁴

1.6.2. Debt-Financing Contracts

The forms in this category are the most used instruments in the Islamic finance industry.¹⁴⁵ This is because from an economic viewpoint, they share many similarities with conventional finance instruments. Moreover, they pose a lower risk in comparison to equity-type instruments.¹⁴⁶ Accordingly, it is not surprising that the

¹⁴¹ Abd Jabbar, "Sharia-Compliant Financial Instruments: Principles and Practice," p176.

¹⁴² El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p120.

¹⁴³ Abd Jabbar, "Sharia-Compliant Financial Instruments: Principles and Practice," p176.

¹⁴⁴ See for example : Usmani, *An Introduction to Islamic Finance*, p37; al-Zuhaylī, *Financial Transactions in Islamic Jurisprudence*, 1, p445.; Munawar Iqbal and David T. Llewellyn eds., *Islamic Banking and Finance : New Perspectives on Profit Sharing and Risk* (Cheltenham, UK; Northampton, MA: Edward Elgar in association with International Association of Islamic Economics, Islamic Development Bank [and] The Islamic Foundation).

¹⁴⁵ See: Usmani, *An Introduction to Islamic Finance*, p65; Samad, Gardner, and Cook, "Islamic Banking and Finance in Theory and Practice: The Experience of Malaysia and Bahrain," p83; Mūsā Ādam ‘isā, " Taṭbīqāt al-Tawaruq wa Astikhdāmātuh fī al-‘amal al-Maṣrifī al-Islāmī " (paper presented at the Dawr al-Mu’sasāt al-Maṣrifīyah fī al-‘astithmār wa al-Tanmiyyah, Sharjah, UAE, 7-9 /5/2002), p463; Sechafia et al., "What Drives An Ideal Islamic Finance? A Maqasid Compliance Approach," p11-13.

¹⁴⁶ Samad, Gardner, and Cook, "Islamic Banking and Finance in Theory and Practice: The Experience of Malaysia and Bahrain," p75; Salman Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?," Institute of Islamic Banking and Insurance, <http://www.newhorizon-islamicbanking.com/index.cfm?section=academicarticle&action=view&id=10735>. accessed 18 May 2013.

Shari‘ah compliance of some of these instruments is very controversial among Shari‘ah scholars, since they are seen as deviating from the objectives of Shari‘ah.¹⁴⁷

Although this category includes many instruments, this section briefly describes the most common ones in the industry, namely *murābahah*, *tawarruq*, and *īnah*.

Murābahah (a mark-up sale)¹⁴⁸ is a form of finance where a client orders the bank to buy a commodity or property with a binding promise to buy it from the bank. The bank then sells it to the client via deferred payment at a cost that includes a profit margin.

*Tawarruq*¹⁴⁹ is defined in the Islamic jurisprudence literature¹⁵⁰ as a form of finance where buyer A purchases a commodity from a seller for a deferred payment and then resells it to buyer B for cash at a price that is usually lower than the original cost. Buyer A does not intend to use the commodity, but rather purchases it intending to sell it to obtain liquidity. Buyer A does not have a prior arrangement to sell the commodity to a specific buyer B in this case. Chapter 3 examines *tawarruq* as a case study for creative Shari‘ah compliance.

*Bai' al-‘ina*¹⁵¹ is a form of finance where an owner sells his asset on a deferred basis and then buys it back from the purchaser on a cash basis at a price that is usually lower than the original selling price. While the owner profits from the difference between the first purchase price and the buyback price, the first buyer secures liquidity without engaging directly in a usurious loan. However, the majority of

¹⁴⁷ In addition to the discussion on *tawarruq* in chapter five, see: El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p2; El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p133; Usmani, *An Introduction to Islamic Finance*, p72.

¹⁴⁸ Khan, *Islamic Economics and Finance : a Glossary*, p26 ; El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p64-68; al-Zuhaylī, *Financial Transactions in Islamic Jurisprudence*, 1, p354.

¹⁴⁹ Khan, *Islamic Economics and Finance : a Glossary*, p182.

¹⁵⁰ While the term “*tawarruq*” has been mainly used by the Hanbalī School, other schools of thought have included this contract under *īnah* transaction. See: Abdullah Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyyah* (Riyadh: Dār Kunūz Ashbīliyyā, 2011), P14.

¹⁵¹ Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p39.

Shari‘ah scholars deem such a transaction as *muḥarram* (prohibited) because they see it as *ḥīlah* (a legal ruse) to circumvent the Shari‘ah prohibition against *ribā* (usury).¹⁵² Chapters two and three provide more insight about these types of transactions.

1.7. The Objectives of Islamic Law

A study of the objectives of Shari‘ah law, known in Arabic as *maqāṣid al-sharī‘ah*, is necessary to properly identify practises of creative Shari‘ah compliance in the Islamic finance industry.¹⁵³ How can we know that a particular transaction does not comply with the objectives of the law if we do not know these objectives? In addition, knowing *maqāṣid al-sharī‘ah* is a significant tool for assessing the justifications used for some creative Shari‘ah compliance practises.¹⁵⁴ As will be seen later, the objectives of Shari‘ah can be divided into different levels which have different priorities. In some situations, a low-priority objective of Shari‘ah has been used as an excuse not to conform to a rule that serves a higher objective of Shari‘ah.¹⁵⁵ For example, the usury prohibition serves two higher objectives of Shari‘ah, which are to circulate and protect wealth as well as to remove social injustice. A lower-priority objective of Shari‘ah, removing hardship, has been used to justify some circumventions of the usury prohibition, although these practises violate the two higher objectives of Shari‘ah that are associated with the prohibition.¹⁵⁶

¹⁵² See: El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p44.; Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p39.

¹⁵³ Khaf notes that “from a financial-cum-economic point of view, the lack of full observance of the objectives of the prohibition of Riba may render a hybrid contract into a mere superficial cover up of what is prohibited and makes Islamic financing completely ineffective and inefficient in performing its essential characteristics.” Monzer Kahf, "Maqasid al Shari'ah in the Prohibition of Riba and their Implications for Modern Islamic Finance" (paper presented at the IIUM International Conference on Maqasid al Shari'ah, Kuala Lumpur, Malaysia, 8-10/8/2006), p14.

¹⁵⁴ See: Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari`ah in Islamic Banking and Finance," p3.

¹⁵⁵ See: Al-Mubarak and Osmani, "Applications of Maqasid al-Shari'ah and Maslahah in Islamic Banking practices: An Analysis," p1.

¹⁵⁶ Abozaid and Dusuk discuss this point under the heading of “Macro Maqasid versus Micro Maqasid.” See: Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari`ah in Islamic Banking and Finance," p3 also p8 & p19.

Accordingly, identifying which objective prevails over another is crucial to refuting such justifications.

Maqāṣid al-sharī‘ah has almost become a separate discipline within Islamic legal theory, with a vast collection of classical and modern literature directed to this subject. As the limited scope of this thesis does not allow a thorough introduction to *maqāṣid al-sharī‘ah*, it gives readers a brief overview of the subject here. *Maqāṣid* in Arabic is the plural of *maqṣad*, which can be translated as “destination, intent, purpose, object, goal, aim, and end”.¹⁵⁷ *Maqāṣid al-sharī‘ah* consists of the wisdom and underlying objectives of Shari‘ah rulings.¹⁵⁸ Muslim legal theorists agree that the overall objective of Shari‘ah is to bring benefit to and remove harm from all human beings.¹⁵⁹ Abū Ḥāmid al-Ghazālī¹⁶⁰ (d. 505 AH/1111 CE), one of the most notable Muslim legal theorists, gives a more detailed account of this overall objective of Shari‘ah. He holds that Shari‘ah promotes the well-being of people by protecting five principles: the preservation of religion (*dīn*), the preservation of life (*naḥs*), the preservation of intellect (*‘aql*), the preservation of posterity (*nasl*), and the preservation of wealth (*māl*). According to al-Ghazālī, anything that contributes to the preservation of these five principles benefits the public and is desired, while anything that harms them is detrimental to the public and should be eliminated. These five elements identified by al-Ghazālī have become known in Islamic legal theory as the five essential *maqāṣid* (objectives).

¹⁵⁷ Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p2.

¹⁵⁸ Mirza Vejjagic and Edib Smolo, "Maqasid Al-Shari'ah in Islamic Finance: An Overview" (paper presented at the The 4th Islamic Economic System Conference 2011 (IECONS 2011), Kuala Lumpur, Malaysia, 4-5 /10/ 2011), p4.

¹⁵⁹ Asyraf Wajdi Dusuki and Said Bouheraoua, *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance* (Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA),, 2011), p3. Mohamad Akram Laldin and Hafas Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)* (Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2012), p8.

¹⁶⁰ Abū Ḥāmid al-Ghazālī *al-Mustasfā fī ‘alm al-Uṣūl*, vol. 1 (al-Risālah, 1997), p416.

Dusuki and Bouheraoua¹⁶¹ identify four main characteristics of *maqāṣid al-sharī‘ah*. The first is that they are regarded as the foundation of legislation. This is because laws aim to benefit the public and protect against harm. Any rule that does not serve this purpose is not part of Shari‘ah, even if some interpretations claim it to be. Shari‘ah jurists have arrived at this conclusion through an inductive reading (*istiqrā’*) of the primary sources of Shari‘ah. Dusuki and Bouheraoua quote the following statement of Ibn al-Qayyim (d.751/1350):

The Shari‘ah is based on wisdom and achieving people’s welfare in this life and in the hereafter. The Shari‘ah is all about justice, mercy, wisdom, and good. Thus, any ruling that replaces justice with injustice, mercy with its opposite, common good with harm, or wisdom with nonsense, is a ruling that does not belong to the Shari‘ah even if it is claimed to be so according to some interpretations.¹⁶²

The second characteristic of *maqāṣid al-sharī‘ah* is its universal nature, given that Shari‘ah is meant to benefit all human beings. Islam is not restricted to certain groups of mankind, and Muslims believe that Shari‘ah is applicable to all people until the end of this world. Verse 34:28 reads, “We have not sent you, [O Muhammad,] except to mankind as a whole”.¹⁶³ The third characteristic of *maqāṣid al-sharī‘ah* is its applicability to all human deeds, from a personal act of worship of god to an interaction with other human beings. Verse 16:89 reads, “And we sent down to you the Book as a clarification for everything and as guidance and a mercy and good tidings to the Muslims”.¹⁶⁴ The fourth characteristic of *maqāṣid al-sharī‘ah* is that it is comprehensive, in the sense that it has been based on different collections of legal texts, as opposed to rules that are based on a single item of legal evidence. Dusuki and Bouheraoua provide several examples of legal maxims in Islamic legal theory which

¹⁶¹ Dusuki and Bouheraoua, *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance*, p7.

¹⁶² Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p3.

¹⁶³ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

¹⁶⁴ Ibid.

have this characteristic, such as *al-umwr bimaqāshidihā* (“Acts are judged by intentions”), *al-kharāj biāldamān* (“The right to gain and profit comes with liability to loss and damage”), and *al-darūriyāt tubḥ al-mahzūrāt* (“Necessity legalises prohibitions”).

Islamic legal theorists divide the objectives of Islamic law into two categories, *maqāshid ‘āmmah* (general objectives) and *maqāshid khāṣṣah* (specific objectives).¹⁶⁵ While the former provides the overall objectives for the whole legal system, the latter presents the aims of a particular aspect of Islamic law—for example, the objectives of Islamic finance or of Shari‘ah criminal law. However, considering the great deal of intersection and integration between the general and specific objectives of Islamic law, dealing with these categories in a discrete way might be naïve.¹⁶⁶

Al-Shāṭibī (d.790/1388),¹⁶⁷ a renowned classical theorist in the area of *maqāshid al-shari‘ah*, further subdivides the general objectives of Shari‘ah into three groups based on a hierarchy of importance: *darūriyāt* (the necessities), *hājjiyyāt* (the complementary or the needs), and *taḥṣīynāt* (the luxuries).¹⁶⁸ The necessities group, comprising elements that are essential to human welfare, includes the five objectives of al-Ghazālī mentioned earlier: safeguarding religion, life, intellect, posterity, and wealth.¹⁶⁹ Other scholars have added objectives to this category, including protecting justice, equality, freedom and the environment.¹⁷⁰ The safeguarding of these elements

¹⁶⁵ See: Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p5. Gamal Eldin Attia, *Towards Realization of the Higher Intents of Islamic law : Maqasid al-Shari‘ah : a functional approach*, trans. Nancy Roberts (London [etc.]: International Institute of Islamic Thought, 2007), p113.

¹⁶⁶ Dusuki and Bouheraoua, *The Framework of Maqasid Al-Shari‘ah (Objectives of the Shari‘ah) And Its Implications in Islamic Finance*, p11.

¹⁶⁷ Ibrāhīm Mūsā al-Shāṭibī, *al-Muwāfaqāt*, ed. Mashhūr Ḥasan Salmān, vol. 2 (Dār Ibn ‘Affān, 1997), p17.

¹⁶⁸ Vejzagic and Smolo, "Maqasid Al-Shari‘ah in Islamic Finance: An Overview," p6.

¹⁶⁹ Mohammad Hashim Kamali, "Al-Maqasid Al-Shari‘ah: The Objectives Of Islamic Law," *The Muslim Lawyer Journal* 3, no. 1 (1998): p2.

¹⁷⁰ See: Attia, *Towards Realization of the Higher Intents of Islamic law : Maqasid al-Shari‘ah : a functional approach*, p17 &77; Laldin and Furqani, *Developing Islamic Finance in the Framework of*

is crucial to the well-being of individuals and society in both religious and worldly matters; the erosion of these elements can result in disorder and chaos.¹⁷¹ The second group, *ḥājīyyāt*, includes elements of a lower priority than the five core elements in the first category. The fulfilment of these objectives eliminates hardship and predicament while facilitating daily life. Unlike the necessities group, neglecting these elements will not lead to disorder and chaos.¹⁷² The group of *taḥsīyynāt* (luxuries or embellishments) includes interests oriented toward improving life, as well as good conduct and actions such as donating to the needy beyond the compulsory *zakah*. These three groups are interconnected.¹⁷³ The necessities are vital to the needs and luxuries groups, as any scarcity in the first group unavoidably results in scarcities in the second two groups. Similarly, a complete shortage in the needs and luxuries groups might result in scarcity to some extent in the necessities group.

The management of institutions offering Islamic financial services (IIFS) should consider how their decisions and actions will affect the interests of the three groups. For example, IIFS should not become involved in a business that could hurt one of the five essentials, such as the manufacturing of drugs and alcohol, which can hurt intellect and life. Similarly, investing in a casino breaches the objectives of preserving religion and wealth. At the second level, the complementary, IIFS should ensure adequate training, fair pay and comfortable workplaces for their employees. These amenities will remove hardship, although their absence will not directly hurt the essential five elements. At the third level, the embellishments, IIFS can fulfil their

Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il), p10; Auda, *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*, p6.

¹⁷¹ Dusuki and Bouheraoua, *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance*, p10.; Kamali, "Al-Maqasid Al-Shari'ah: The Objectives Of Islamic Law," p2.

¹⁷² See: Muhammad al-Tahir Ibn `Ashur, *Ibn Ashur : treatise on Maqasid al-Ahari'ah* (Herndon, VA.: International Institute of Islamic Thought, 2006), p123.; Vejzagic and Smolo, "Maqasid Al-Shari'ah in Islamic Finance: An Overview," p7.

¹⁷³ Dusuki and Bouheraoua, *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance*, p11.

social responsibility and contribute to the improvement of public life via such mechanisms as donations and sponsorship of charitable events.¹⁷⁴

With regard to the objectives of Islamic finance, Shari‘ah theorists tend to centralise their discussion on the notion of wealth protection, as pointed out by al-Ghazālī,¹⁷⁵ and wealth circulation. The circulation of wealth initiates with the mobilisation of surplus capital and continues until the capital is utilised in the deficit sector. The circulation of wealth includes all procedures associated with its creation, utilisation and allocation. The objective of wealth circulation is drawn from verse 59:7 of the Quran, which justifies the command of distributing a person’s wealth among different needy groups in society “in order that it [wealth] may not [merely] make a circuit between the [rich] among you”.¹⁷⁶ Shari‘ah aims to circulate resources in the economy so that individuals can fulfil their potential to foster the well-being of the community and future generations.¹⁷⁷ Wealth is deemed Allah’s bounty, which mankind is entrusted¹⁷⁸ to allocate in the best possible way. Kamali¹⁷⁹ notes that *’adl* (justice) has been mentioned in the Quran 53 times, which shows that it is a principal objective of Shari‘ah. He explains that *’adl* literally means “to place things in their right and proper order [...] ... [It] is to seek to establish an equilibrium between rights and obligations, so as to eliminate all excesses and disparities, in all spheres of life”. Recognising private ownership does not mean only stratifying personal needs and neglecting the needs of society. Financial transactions and commercial exchanges are

¹⁷⁴ Ibid., p25-26.

¹⁷⁵ See: Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari’ah: Understanding the ends (maqasid) and the means (wasa’il)*, p12; Sechafia et al., "What Drives An Ideal Islamic Finance? A Maqasid Compliance Approach," p7.

¹⁷⁶ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

¹⁷⁷ Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari’ah: Understanding the ends (maqasid) and the means (wasa’il)*, p13.

¹⁷⁸ See: Mustafa Omar Mohammad and Syahidawati Shahwan, "The Objective of Islamic Economic and Islamic Banking in Light of Maqasid Al-Shariah: A Critical Review," *Middle East Journal of Scientific Research* 13(2013): p76.

¹⁷⁹ Kamali, "Al-Maqasid Al-Shari’ah: The Objectives Of Islamic Law," p1.

seen as a means of circulating resources among all parts of the community and are not to be dominated by a small group of people.¹⁸⁰ In other words, social justice is realised in Shari'ah via resource circulation, efficiency in resource consumption, and the satisfaction of people's basic needs.

In addition, Shari'ah scholars have affirmed the safeguarding of wealth in several key dimensions such as preserving ownership, preserving the value of wealth, protecting wealth from damage,¹⁸¹ associating transactions with real economic activities, and prohibiting the sale of debt. A Shari'ah legal principle such as *al-kharāj bi'l-damān* (the right to gain and profit comes with liability to loss and damage) reflects the spirit of social justice which Islamic finance tries to achieve.¹⁸²

The prohibition of *ribā* and *gharar* serves to achieve the same result of social justice. *Ribā* is seen as unjustified growth in wealth and has been associated with wrongful acquisition at the cost of the fair circulation of resources, as well as the welfare of the public.¹⁸³ The prohibition of *riba* suggests that Shari'ah encourages cooperative and participatory funding (equity-based financing), which is thus regarded as a fair mechanism for mobilising wealth which increases productivity and achieves social well-being.¹⁸⁴ Moreover, by preventing negative factors such as *ribā* and *gharar* that disturb equality or give one party the chance to increase its wealth at

¹⁸⁰ Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)*, p13.

¹⁸¹ Dusuki and Bouheraoua, *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance*, p12.

¹⁸² Ahmed, "Maqasid al-Shari'ah and Islamic Financial Products: A Framework for Assessment," p150.

¹⁸³ For an extenuative discussion of the harm of *ribā* see: El Diwany, *The Problem With Interest*; M. Umer Chapra, "The Case Against Interest: Is It Compelling?," *Thunderbird International Business Review* 49, no. 2 (2007); Mohammad Nejatullah Siddiq, "The Wisdom of Prohibition of Interest," www.siddiqi.com, http://www.siddiqi.com/mns/Interest_Prohibition.html. accessed 1 March 2014; Kahf, "Maqasid al Shari'ah in the Prohibition of Riba and their Implications for Modern Islamic Finance."

¹⁸⁴ See: Eddy Yusof, Kashoogie, and Anwar Kamal, "Islamic Finance: Debt versus Equity Financing in the Light of Maqasid al-Shari'ah." p1.; Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)*, p17. Vejzagic and Smolo, "Maqasid Al-Shari'ah in Islamic Finance: An Overview," p13.

the expense of others, Shari'ah aims to establish a level playing field between different parties in a transaction. One of the main characteristics of *ribā* is that it shifts risk to one party while protecting the other with a fixed return. In a usurious loan, risk is transferred to the borrower, who is required to pay the capital plus interest regardless of any loss that he may incur.¹⁸⁵ The widespread practise of interest-based loans increases debt proliferation, which has harmful effects that Shari'ah aims to remove.¹⁸⁶ Siddiqi¹⁸⁷ argues that a financial system based on debt is unfair because it redistributes wealth in favour of the providers of finance regardless of the productivity of the fund provided. It is also an inefficient way of creating wealth, since the fund goes to the most creditworthy debtor and not to the most productive project. He also notes that

To exchange money now for more money later is fundamentally unfair due to the uncertainty that accompanies the passage of time. Money needs to be converted into goods and services before it can enter into the process of production, the source of possible additional value creation. The results of such process[es] of production have to be reconverted into money before money can be paid back to the one who gave it in the first instance.¹⁸⁸

On the other hand, *gharar* is forbidden due to its impact on efforts to negotiate a fair financial contract.¹⁸⁹ This is because the uncertainty surrounding the subject of the contract in terms of its existence, possession, availability, price, and deliverability increases the role of pure speculation and leaves one party to the transaction

¹⁸⁵ "Maqasid Al-Shari'ah in Islamic Finance: An Overview," p9.; Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)*, p20.

¹⁸⁶ Asyraf Wajdi Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?* (Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2010), p12. E Fahmy et al., "Revisiting OIC Fiqh Academy Rules on Organised Tawarruq," (2008) <http://www.scribd.com/doc/21445765/Revisiting-OIC-Fiqh-Academy-Rules-on-Organised-Tawarruq> accessed 10 November 2013.

¹⁸⁷ Siddiq, "Economics Of Tawarruq: How Its Mafasid Overwhelm The Masalih" p1-2.

¹⁸⁸ Ibid., p2. He further points out that debt-based financing causes economic instability since "in a debt-based economy, the money supply is linked to debt with a tendency towards inflationary expansion" (p7).

¹⁸⁹ See: Laldin and Furqani, *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)*, p20.

dissatisfied and disappointed. This in turn causes harm and tends to lead to disputes.¹⁹⁰

1.8. Conclusion

This chapter has provided an overview of Islamic law and its key features to prepare readers for a substantive discussion of their application in the Islamic financial industry in subsequent chapters. The policies and objectives of IIFS, as businesses based on Shari‘ah-compliant products, should be strongly influenced by the objectives of Islamic law. Moreover, these objectives should be used as criteria to assess the compliance of IIFS with Shari‘ah principles. Thus, understanding the sources, principles, distinctions, and organisation of Shari‘ah law is crucial to understanding this thesis’s discussion of creative Shari‘ah compliance.

The next chapter, “The Form Versus Substance Debate and the Roots of Creative Shari‘ah Compliance in Islamic Finance: Why Reinvent the Wheel?” draws on this foundational information to examine whether creative Shari‘ah compliance is a phenomenon new to Islamic law. It investigates the positions of the various schools of thought on issues related to “substance” and “form” in Islamic finance, and it surveys whether classical Islamic jurisprudence justifies using *ḥīlah* (a legal ruse) to practise creative Shari‘ah compliance.

¹⁹⁰ El Diwany, *Islamic Banking and Finance : What it is and What it could be*, p114.

Chapter Two:

The Form Versus Substance Debate and the Roots of Creative Shari‘ah Compliance in Islamic Finance: Why Reinvent the Wheel?

You should never neglect the intention of the speaker and his motives; if you do, you would harm him, and you would harm the Shari‘ah by attributing to it something that does not befit it. A sound-minded jurist would ask, “What did you intend?” and a shallow-minded jurist would ask, “What did you say?”¹⁹¹

—Ibn al-Qayyim (d.751 AH/1350 CE)

2.1. Introduction

The issue of financial contracts’ legal form versus their economic and ethical substance has been frequently debated in the Islamic finance industry.¹⁹² It has recently attracted more attention after the outcome of several English cases which called into question the enforceability of some contracts widely used to structure Islamic financial products.¹⁹³ In 2011,¹⁹⁴ the International Shari‘ah Research Academy

¹⁹¹ Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p53.

¹⁹² See for example: El-Gamal, *Islamic Finance : Law, Economics, and Practice*; Haider Ala Hamoudi, "Jurisprudential Schizophrenia: On Form and Function in Islamic Finance," *Chicago Journal of International Law* 7, no. 2 (2007); Habib Ahmed, "Islamic Finance at a Crossroads: the dominance of the asset-based sukuk," *Butterworths Journal of International Banking and Financial Law*. 25, no. 6 (2010); Richard de Belder, "Form Over Substance – Will the Secular Courts Force the Issue?," *Newhorizon* 2011; Khalid Howladar, "The Future of Sukuk: Substance over Form?," Moody’s Investors Service, <http://www.kantakji.com/fiqh/Files/Markets/m170.pdf>. accessed 30 October 2012; Muhammad Ismail, "'Substance' over 'Form' in Islamic Finance: Analysis of Murabaha and Ijara Contracts," *Newhorizon*, <http://www.newhorizon-islamicbanking.com/index.cfm?section=iibinews&action=view&id=10825>. accessed 30 October 2012; Maurer Bill, "Form Versus Substance: AAOIFI Projects and Islamic Fundamentals in the Case of Sukuk," *Journal of Islamic Accounting and Business Research* 1, no. 1 (2010).

¹⁹³ For extensive analyses see: Nicholas H. D. Foster, "Islamic Finance Law as an Emergent Legal System," *Arab Law Quarterly* 21, no. 2 (2007); Kilian Bälz, "A Murabaha Transaction in An English Court - The London High Court of 13th February 2002 in Islamic Investment Company of the Gulf (Bahamas) Ltd. V. Symphony Gems N.V. & Ors," *Islamic Law and Society* 11, no. 1 (2004); Hakimah Yaacob, "A Critical Appraisal of International Islamic Finance Cases and the Way Forward," *ISRA Research Paper No. 19/2011*(2011) <http://www.isra.my/media-centre/downloads/view.download/29-isra-research-paper/293-a-critical-appraisal-of-international-islamic-finance-cases-and-the-way-forward-no-192011.html> accessed 30 October 2012.

¹⁹⁴ Institute of Islamic Banking and Insurance (IIBI), "3rd Annual ISRA/IIBI Thematic Workshop: Monday, 12th December 2011," http://www.islamic-banking.com/resources/1/Workshops%202011/IIBI-ISRA%20SNR%20DENTON%20WS%202011%20ver%204_invite%20reduce%20only.pdf. accessed 10 May 2012.

Academy for Islamic Finance (ISRA) and the Institute of Islamic Banking and Insurance (IIBI) organised a thematic workshop where Shari‘ah scholars, lawyers, and practitioners gathered to discuss the challenges of form versus substance in Islamic finance transactions and to assess how credibility could be restored to allay concerns about authenticity in the Islamic finance industry.

However, as this chapter shows, the debate of form and substance is not completely new to Islamic law literature, though it has been addressed using different terminology. Classical jurists have extensively debated the issue using the term *ḥīlah* (legal ruse).¹⁹⁵ It is not clear why the term *ḥīlah* is avoided when the issue arises in some of the contemporary literature, conferences, and workshops such as the one mentioned earlier. Is it because the subject is sensitive and the word *ḥīlah* might be offensive, since it implies a sense of deception, or is it because the usage might cause harm to the marketing of Islamic financial products? Whatever the reason, disguising a known issue in the literature under new terminology does not take the debate forward. Accordingly, this chapter recognises that discussing the issue of form versus substance in Islamic finance is basically discussing *ḥīlah*. This chapter therefore aims to examine the treatment of *ḥīlah* in *sunni* Islamic jurisprudence, and it surveys whether classical Islamic jurisprudence justifies using *ḥīlah* to practise creative Shari‘ah compliance.

This chapter’s key argument is that addressing the issue of form and substance in Islamic finance necessitates a distinction between two connotations: permissibility (*ṣaḥīḥ diyānatan*) and validity (*ṣaḥīḥ qaḍā’an*).¹⁹⁶ In Islam, every action generally

¹⁹⁵ See: al-Shāṭibī, *al-Muwāfaqāt*, 1, vol 3 p124; Ibn Taymiyah, *Bayān al-Dalīl ‘alā Iḥṭā’ al-Taḥlīl*, p159. Ibn al-Qayyim, *I’lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p240; Ayub, *Understanding Islamic Finance*, p147.

¹⁹⁶ See on the issue of permissibility (*ṣaḥīḥ diyānatan*) and validity (*ṣaḥīḥ qaḍā’an*). Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari‘ah in Islamic Banking and Finance," p15. Refer also to chapter one (Islamic Legal Ruling) at p21.

has two dimensions: hidden and manifest. “Permissibility” here refers to the inward, hidden dimension of a contract, where it is characterised, for example, as prohibited or permissible. This dimension concerns the accountability of a person to Allah in the hereafter. “Validity”, in this research, refers to the outward, manifest dimension of a contract, where a judge rules whether it is valid and thus legally enforceable or not. The outward dimension is concerned with individuals’ rights in this world. From a permissibility perspective, the research argues that there is no authority for utilising a form to circumvent the spirit of Shari‘ah law in finance. However, from a judicial validity perspective, if such a form had been used in a contract and disputed before a judge, it could be deemed valid according to some schools of thought, including Ḥanafī and Shāfi‘ī.

The chapter is structured in six parts including this introduction. Part 2.2 briefly explores definitions of *ḥīlah* in Islamic jurisprudence; Part 2.3 addresses the causes and the origin of *ḥīlah*; Part 2.4 investigates the view of Islamic schools of thought on *ḥīlah*; Part 2.5 examines the arguments for and against *ḥīlah*; finally, Part 2.6 concludes the chapter.

2.2. The Definition of *Ḥīlah*

Ḥīlah (plural *ḥīyal*) can be defined as a legal ruse or stratagem which uses legitimate means to achieve illegitimate ends.¹⁹⁷ By applying a formalistic approach to contracts, it complies with the letter of the Shari‘ah while circumventing its substance.¹⁹⁸ For example, to evade the Shari‘ah prohibition of collecting interest on

¹⁹⁷ See: Koutoub Moustapha Sano, *Mu‘jam Muṣṭalahāt Uṣūl al-Fiqh* (Damascus: Dar al-Fikr, 2000), p190; Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p160; Noel J. Coulson, *A History of Islamic Law* (Edinburgh: Edinburgh University Press, 2003), p139.

¹⁹⁸ Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p39.

loans, the lender would use an *ṭinah* contract,¹⁹⁹ which involves double selling as follows: the lender sells a commodity to a prospective debtor for a fixed price on a deferred payment basis, and then buys it back immediately for cash at a lower fixed price. The debtor gets the cash he needs, while the lender keeps the asset used in the transaction in addition to the original purchase price, with a profit element which will be paid in instalments. In this example, the sale contracts in form appear to be Shari‘ah compliant because each transaction is separately a legitimate contract, but the complete process of the two transactions achieves an illegitimate end, which is charging interest on a loan. The debtor does not intend to purchase the asset, and the lender usually uses the same commodity to complete this procedure with other prospective debtors.

However, it is important to point out that the same word has been used with a different meaning in the classical and contemporary literature. The word *ḥīlah* can also refer to a clever way of using the law which achieves a legitimate end.²⁰⁰ Al-Sha‘bī (d.104 AH/722 CE), for example, defines *ḥīlah* as a tactic in which a person can take a permissible action and avoid breaching prohibition and committing sins.²⁰¹ The original root of the word in Arabic justifies such use.²⁰² However, other scholars such as Ibn Taymiyah (d.728/1328), Ibn al-Qayyim (d.751/1350), and al-Shāḥibī (d.790/1388) use the term for both meanings, but add the qualifications of reprehensible *ḥīlah* and commendable *ḥīlah* to differentiate between the two

¹⁹⁹ There are different forms and definitions of *ṭinah* contract; the most famous one is a double sale allowing the collection of interest. See: ‘abdAllāh al-Sa‘īdī, "Madhāhib al-Fuqahā’ fī al-ṭinah," *al-Dr‘īyyh* 7, no. 26 (2004).

²⁰⁰ See: Muḥammad Ibrāhīm, *al-Ḥiyal al-Fiḥhiyyah fī al-Mu‘āmalāt al-Māliyyah* (Dar Alsalam, 2008), p20. Joseph Schacht, *An Introduction to Islamic Law* (Oxford: Oxford University Press, 1982), p79; Muḥammad Sa‘īd al-Būṭī, *Ḍawābiṭ al-Maṣlaḥah fī al-Sharī‘ah al-Islāmiyyah* (Mu‘assisah al-Risālah, 1973), p293.

²⁰¹ al-Khaṣṣāf, *Kitāb al-Ḥiyal*, p4.. See also: Aḥamad al-Ḥamawī, *Ghamz ‘Uyūn al-Baṣā’ir Sharḥ Kitāb al-‘Ashbāh wa al-Nazā’ir*, vol. 2 (Dār al-Kutub al-‘Ilmiyyah, 1985), p19.

²⁰² Ibrāhīm, *al-Ḥiyal al-Fiḥhiyyah fī al-Mu‘āmalāt al-Māliyyah*, p18.

usages.²⁰³ The former serves to conclude illegitimate ends, whereas the latter achieves a result that does not contradict the spirit of the law. Contemporary scholars seem to favour referring to the permissible *ḥīlah* with the term *makhraj fiqhī* (jurisprudential leeway),²⁰⁴ while using “*ḥīlah*” to refer to an unlawful ruse.²⁰⁵

2.3. The Origins and the Evolution of *Ḥīlah*

The use of legal ruses to comply with the letter of the law is a phenomenon not limited to one society;²⁰⁶ legal stratagems have been used in different legal systems throughout history.²⁰⁷ In the Islamic context, Ibn Taymiyah²⁰⁸ notes that the advocating of *ḥīlah* only started after the first Islamic century (700–740 AH). Several theories have been advanced as to why *ḥīlah* developed in Islamic societies.²⁰⁹ Given its limited space, this chapter discusses the three most commonly cited theories, namely, the excessive use of hypothetical cases as a method of teaching Islamic jurisprudence; political conflicts and state oppression; and the gap between the ideology of Shari‘ah and the needs of the society.

²⁰³ See: al-Shātibī, *al-Muwāfaqāt*, 1, vol 3 p124; Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p159. Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p240..

²⁰⁴ The term *makhraj fiqhī* was also used in classical jurisprudence. See Zayn al-‘ābidin Ibrāhīm Ibn Nujaym, *al-‘ashbāh wa al-naẓā‘ir*, ed. Muḥammad Muṭī‘ al-Ḥāfīz, 2nd ed. (Dār al-Fikr, 2005).

²⁰⁵ Arieff Salleh Rosman, "al-Ḥiyal wa al-Makhārij fī al-Mu‘āmalāt al-Maṣrifīyah al-Islāmiyyah" (PhD thesis International Islamic University of Malaysia, 2008), p39.. Ibn Taymiyah acknowledged that in the language of *fuqahā’*, *ḥīlah* has become a term for prohibited artifice. See: Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p159.

²⁰⁶ See: Coulson, *A History of Islamic Law*, 140; S.G. Vesey-Fitzgerald, "Nature and Sources of the Sharī‘a," in *Law in the Middle East*, ed. Majid Khadduri and Herbert J. Liebesny (Washington: The Middle East Institute, 1955), 106; Fāḍil al-Ḥusaynī al-Milānī, "al-Ifṭirāḍ al-Qānūnī wa al-Ḥīlah al-Sharī‘iyah," Almilani, <http://almilani.org/%D8%B9%D8%B1%D8%A8%D9%8A/%D8%A7%D9%84%D9%85%D9%82%D8%A7%D9%84%D8%A7%D8%AA/696>. accessed 18 April 2012.

²⁰⁷ Craig Nethercott and David Eisenberg, *Islamic Finance: Law and practice* (Oxford: Oxford University Press, 2012), p48.

²⁰⁸ Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p126.

²⁰⁹ See: Rafiq Ūnis al-Maṣrī, "al-Ḥīl al-Fiqhiyyah bayn al-Būṭī wā Ibn Qaim al-Jawziyyah," Islamic Economic Research Centre, http://islamiccenter.kau.edu.sa/arabic/Hewar_Arbeaa/abs/263/Hiwar1430-16.pdf. accessed 10 May 2012; Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu‘āmalāt al-Māliyyah*, p57; Rosman, "al-Ḥiyal wa al-Makhārij fī al-Mu‘āmalāt al-Maṣrifīyah al-Islāmiyyah," p65; Joseph Schacht, "Ḥiyal," in *Encyclopaedia of Islam* (Brill 2012) <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/hiyal-SIM_2913> accessed 1 April 2012; Vesey-Fitzgerald, "Nature and Sources of the Sharī‘a," p106.

2.3.1. *The Excessive Use of Hypothetical Cases*

Historically, different schools of thought commonly used hypothetical questions as method of teaching Islamic jurisprudence.²¹⁰ In particular, the Ḥanafī School in Iraq was famous for discussing legal challenges and speculating about situations that might arise in the future.²¹¹ However, the heavy engagement of Ḥanafī jurists in this practise led to the development of imaginary cases where the use of *ḥīlah* was the only legally valid solution. Although these discussions and debates were more of a scholastic nature and were not necessary presented as *fatwas*, they eventually become a part of the school's jurisprudence and were used by the following generation of jurists as grounds for issuing *fatwas*.²¹²

Most of these *ḥīyal* initially involved questions about how to avoid obligations committed under vows or oaths.²¹³ Historically, some rulers tended to force people, particularly political dissenters, to swear an oath of allegiance to ensure their loyalty. In addition, it was a common practise in the early Islamic centuries for a person to impose a penalty on himself if he did not fulfil his oath or vow. Another widespread practise was for a person to declare the divorce of his wife or the manumission of his slave subject to the happening of "a certain event, such as: if I do such and such a thing, or if such and such a thing happens, my wife is repudiated, or my slave is manumitted".²¹⁴ Shari'ah generally discourages using an oath or vow in such a way but obligates its fulfilment once it has been undertaken. Therefore, *ḥīlah* was sought

²¹⁰ Ibrāhīm, *al-Ḥiyal al-Fiḥiyyah fī al-Mu'āmalāt al-Māliyyah*, p58; Rosman, "al-Ḥiyal wa al-Makhārīj fī al-Mu'āmalāt al-Maṣrifīyyah al-Islāmiyyah," p71; Ignác Goldziher, *Introduction to Islamic Theology and Law*, trans. Andras Hamori and Ruth Hamori (Princeton, N.J.: Princeton University Press, 1981), p63.

²¹¹ Ibrāhīm, *al-Ḥiyal al-Fiḥiyyah fī al-Mu'āmalāt al-Māliyyah*, p58; Rosman, "al-Ḥiyal wa al-Makhārīj fī al-Mu'āmalāt al-Maṣrifīyyah al-Islāmiyyah," p71; Goldziher, *Introduction to Islamic Theology and Law*, p63.

²¹² See: Aḥmad Amīn, *Ḍuḥā al-Islām*, vol. 2 (al-Hay'ah al-'Āmah al-Maṣrīh lil-Kitāb, 1998), p191.

²¹³ See: Goldziher, *Introduction to Islamic Theology and Law*, p65; Amīn, *Ḍuḥā al-Islām*, 2, p191.. Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p33; Schacht, "Ḥiyal."

²¹⁴ Schacht, "Ḥiyal."

to provide relief from the religious and legal duties attached to these oaths. Ibn Taymiyah²¹⁵ cites an incident in which Abū Ḥanīfah (d.150/767) was asked about a man saying to his wife while she was climbing a ladder, “If you go up, you are divorced, and if you come down, you are divorced”. As a way around divorce, Abū Ḥanīfah suggested that others carry the wife off the ladder and put her on the floor. However, as Amīn points out, the practise of *ḥīlah* moved from presuming rare incidents to debating situations and cases that could not possibly happen. In addition, later followers of the school extend these *ḥīyal* from a few vows-related cases to cover other aspects of Islamic jurisprudence.²¹⁶

Such practises, nevertheless, were strongly rejected by scholars such as Mālik Ibn Anas (d.179/795) and Aḥmad Ibn Ḥanbal (d. 241/855) and other figures of the school later known as *ahl al-ḥadīth*²¹⁷ (the traditionalists).²¹⁸ Al-Bukhārī²¹⁹ (d.256/870), in his book *al-ṣaḥīḥ*, allocated a whole chapter objecting to the Ḥanafī School’s view on *ḥīlah*. Moreover, Ibn ‘Abd al-Bar al-Namarī (d.463/1071) reports numerous incidents in which a person would ask a renowned scholar about his *fatwa* on a case or situation, and then the scholar would ask, “Did it happen?” If the man said no, then he would say, “Leave it until it happens”.²²⁰ Such a position was motivated by a piety that sees issuing *fatwas* as a huge religious responsibility which could hold a scholar accountable to Allah if he made an error in judgment. It is no wonder, then, to see that Ibn Taymiyah links the origin of *ḥīlah* with the promotion of *al-ra’y* (a method of

²¹⁵ Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p33.

²¹⁶ Amīn, *Duḥā al-Islām*, 2, p192.

²¹⁷ The *ahl al-ḥadīth* school includes those who endeavour to base the law on the Prophetic Traditions and the Prophet’s Companions. According to their view, it is illegitimate to favour or solely rely on unrestricted human reasoning, especially when it conflicts with an authentic *ḥadīth*. See Schacht, "Ahl al-Ḥadīth."

²¹⁸ See for example: Sulamān ‘Abd al-Qawī al-Tūfī, *Sharḥ Mukhtaṣar al-Rawḍah*, ed. ‘AbdAllāh ‘Abd al-Muḥsin al-Turkī, vol. 3 (Mu’sasah al-Risāl, 1987), p287; Ibrāhīm Mūsā al-Shāṭibī, *al-Ā’tiṣām*, ed. Salīm ‘Id al-Hilālī, vol. 1 (Dār Ibn ‘Afān, 1992), p137.

²¹⁹ Schacht, "Ḥīyal."

²²⁰ Yūsuf Ibn ‘Abd al-Bar al-Namarī, *Jāmi‘ Bayān al-‘Ilm wa Faḍlih*, ed. Abī al-Ashbāl al-Zaharī, vol. 2 (Dār abn al-Jawzī, 1994), p1054.

reasoning). According to him, most *ḥīyal* were validated by jurists who belonged to the school of *ahl al-raʿy*.²²¹

Another harmful effect of using hypothetical questions as a method of teaching and researching Islamic jurisprudence is that the religious piety and morality of Shariʿah were lost in the course of legal discussion.²²² Scholars and their followers started to investigate actions in question from a purely legal point of view, though those actions had a religious dimension.²²³ People would use *ḥīlah* with a clear conscience as long as it was validated by a scholar, notwithstanding that it might not be considered permissible.

2.3.2. *Political Conflicts and State Oppression*

By the end of the first Islamic century, the Muslim world had experienced several unrests and revolutions. During the ruling of the Umayyad Caliphate (661–750) and the Abbasid Caliphate (750–1258), people in some parts of the Islamic state were forced to swear allegiance to the Caliphate.²²⁴ Jurists were asked about the validity of such forced vows.²²⁵ Some scholars were also persecuted by the authorities due to their political views.²²⁶ For example, Ibrāhīm al-Nakhaʿī (d.95/713), a renowned figure within the *ahl al-raʿy* school, instructed his students to use *tawriyah*

²²¹ Ibn Taymiyah, *Bayān al-Dalīl ʿalā Ibtāl al-Taḥlīl*, p209. The *ahl al-raʿy* school (literally “the people of good sense”) generally includes those in favour of using independent legal argumentation as a method of concluding a Shariʿah ruling. See: Hennigan, "Ahl al-raʿy."

²²² See: Goldziher, *Introduction to Islamic Theology and Law*, p66. Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Muʿāmalāt al-Māliyyah*, p64.

²²³ See: Goldziher, *Introduction to Islamic Theology and Law*, p66. Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Muʿāmalāt al-Māliyyah*, p64.

²²⁴ ʿAbd al-Raḥman Ibn Khuldūn, *Tārīkh Ibn Khuldūn*, ed. Khalīl Shaḥādah, vol. 1 (Dār al-Fikr, 2001), p261.

²²⁵ See: Abu al-Walīd Muḥammad Ibn Rushd, *al-Bayān wa al-Taḥṣīl wa al-Shirḥ wa al-Tawjīh wa al-Taʿlīl limasāʾil al-Mustakhrajah*, ed. Muḥammad Ḥijy, 2ed ed., vol. 18 (Dār al-Gharb al-Islāmī, 1988), p526.

²²⁶ See many examples in: ʿAbū al-ʿArb Muḥammad Aḥmad al-Tamīmī, *Kitāb al-Miḥan*, ed. Yaḥyā Wahy al-Jabbwry, 3ed ed. (Dār al-Gharb al-Islāmī, 2006), p187; ʿAbd al-Ghanī Saʿīd al-Azdī, *Kitāb al-Mutawārīn*, ed. Mashhūr Ḥasan Salmān (Dār al-Qalam 1989).

(misleading double entendres)²²⁷ to protect his hiding place.²²⁸ Later, this established permissibility of using double meanings was used to support the pro-*ḥīlah* argument.²²⁹

In this period of conflict, many people were forced to conclude fictitious transactions to transfer ownership of their property to non-persecuted individuals to protect it from seizure by unjust rulers. A number of *ḥīyal* were formed for this purpose.²³⁰ Classical debates thus arose between different schools of jurisprudence regarding the validity of *bayʿ al-taljiḥ* (fictitious or temporary sale used to avoid seizure by unjust rulers).²³¹

Moreover, to avoid political enmity in this oppressive climate, scholars shifted their interests away from the thorny issues of the day to less threatening theological debates and discussions of implausible legal cases. This environment gradually provided a fertile soil for developing *ḥīlah*.²³²

2.3.3. *The Gap between Shariʿah Ideology and Society’s Needs*

One theory which accounts for the emergence of *ḥīlah* regards it as a natural result of the gap between the idealistic teachings of Islam and the practical needs of Muslim society.²³³ For example, the prohibition of *ribā* and *gharar* (uncertainty) in Islamic commercial law presents an impractical standard, taking into account the needs of

²²⁷ *Tawriyah* generally refers to words or phrases which can be understood in two ways; the listener usually understands the word’s more apparent meaning, but the speaker actually intends the less apparent meaning. See: Li Guo, *The Performing Arts in Medieval Islam* (Leiden; Boston: Brill, 2012).

²²⁸ Ibn al-Qayyim, *Iʿlām al-Mawqīʿ ayn ʿan Rab al-ʿĀlamīn*, 3, p193.

²²⁹ Ibid.

²³⁰ See: Aḥmad al-Ḥaddād, "Maʿāyir al-Tamīz ban al-ʿUqūd al-Ṣūriyyih wa al-Ḥaqiyyiqiyah" (paper presented at the The 10th Conference of Shariʿa Supervisory Boards of Islamic Financial Institutions, Bahrain, 26/5/2010), p12.

²³¹ See: al-Bayān fī Madhhab al-Imām al-Shāfiʿī, *al-ʿUmrānī, Yaḥyā*, ed. Qāsim Muḥammad al-Nūrī, vol. 5 (Dār al-Minhāj, 2000), p105; Muḥammad Amīn Ibn ʿābidīn, *Raddu al-Muḥtār ʿAlā al-Durri al-Mukhtār sharḥ Tanwīr al-Abṣār*, ed. ʿĀdil ʿAbd al-Mawjūd and ʿAlī ʿAwaḍ, vol. 4 (Dār al-Kutub al-ʿIlmiyyah, 2003), vol 5 p273; ʿAbd Allāh Aḥmad Ibn Qudāmāh al-Maqdisī, *al-Mughnī fī Fiqh al-Imām Aḥmad Ibn Ḥanbal al-Shaybānī*, vol. 4 (Dār al-Fikr, 1985), p300.

²³² Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Muʿāmalāt al-Māliyyah*, p57.

²³³ Schacht, *An Introduction to Islamic Law*, p78; Vesey-Fitzgerald, "Nature and Sources of the Shariʿa," p107; Coulson, *A History of Islamic Law*, p138.

business environments.²³⁴ This standard bans any contract which includes uncertain risk, creating economic difficulty for merchants, as according to proponents of this theory, it is not possible for any society to function without a system of usury.²³⁵ According to Khan, pro-*ḥīlah* jurists realised this fact early.²³⁶ Thus, by adhering to the minimum requirements of the letter of the law, *ḥīlah* provided a way of life that balanced the theory with the practical daily needs of Muslim life.²³⁷ At first sight, jurists who advocated *ḥīlah* might be perceived as betrayers of Shari‘ah, when they were supposed to be its guardians.²³⁸ Nonetheless, Coulson²³⁹ argues that those scholars had no choice but to allow *ḥīlah* because it was the only way that the theory could remain a symbol of authority over what was already practised in reality.

However, this account of the origin of *ḥīlah*, mainly advanced by Orientalists,²⁴⁰ is not necessarily convincing.²⁴¹ First, where it was necessary to deal with usury, scholars had a better alternative to inventing *ḥīlah*: namely, directly allowing usurious trading on grounds of necessity. Shari‘ah recognises the maxim that necessity knows no law (*al-ḍarūrāt tubīḥ al-maḥzūrāt*).²⁴² Because that maxim is tied with another legal maxim, “What is permitted due to necessity is restricted to the necessity (*al-*

²³⁴ A *History of Islamic Law*, p138.

²³⁵ See: *ibid.*; Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p239; Schacht, *An Introduction to Islamic Law*, p80.

²³⁶ Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p239.

²³⁷ Schacht, *An Introduction to Islamic Law*, p80.

²³⁸ Coulson, *A History of Islamic Law*, p140.

²³⁹ *Ibid.*

²⁴⁰ There are several definitions of Orientalism, but my use of it here refers to the western appropriation of the literature, language, religion, or thought of eastern cultures to negatively stereotype those cultures and assert western dominance over them. According to Edward Said, Orientalism is an imperialist ideology which constructs “the East” as a monolith, setting up a false binary between “West” and “East” and collapsing the highly diverse cultural traditions of the eastern world into one mythical Other. See: John M. MacKenzie, *Orientalism : History, Theory, and the Arts* (Manchester: New York: Manchester University Press, 1995), p xii.

²⁴¹ See: Coulson, *A History of Islamic Law*, p138; Schacht, *An Introduction to Islamic Law*, p78; Vesey-Fitzgerald, "Nature and Sources of the Shari‘a," p107.

²⁴² See: ‘Alī Aḥmad al-Nadawī, *Mawsū‘ah al-Qawā‘id wa al-Ḍawwābiḥ al-Fiqhiyyah al-Ḥākimah lil-Mu‘āmalāt al-Māliyah*, vol. 1 (Dār ‘Ālm al-Ma‘rifah, 1999), p136; Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p239.

darūrāt tuqaddir biqadarihā)”,²⁴³ this alternative to *hīlah* would discourage people from taking unnecessary debts, because they know that doing so is primarily prohibited and has only been allowed as an exception for a limited time. In contrast, with *hīlah*, people would practise usury with a clear conscience since they are not taking an illegal action.

Second, it is inaccurate to claim that Shari‘ah bans any contract that has any form of uncertain risk. Islam accepts uncertainty to a limited extent in contracts and makes some exceptions to the general prohibition of *gharar*,²⁴⁴ although the details of such exceptions are beyond the scope of this chapter.

Lastly, this account implies that Shari‘ah as law is not suitable to govern the commercial life of Muslims. It is no wonder that many contemporary scholars have strongly criticised such a theory.²⁴⁵ Muslims jurists unanimously agree that Shari‘ah ruling is apt for all times and places.²⁴⁶ Moreover, the argument that no society can function without a system of usury seems untenable.²⁴⁷ A large community of Muslim and non-Muslim traders from the time of the Prophet up until today have managed successful businesses without practicing usury.

2.4. Positions on *Hīlah* of Islamic Schools of Thought

This section examines the treatment of *hīlah* within Islamic jurisprudence, starting with the four major *sunni madhhab* (schools of thought): the Ḥanafī; Shāfi‘ī, Mālikī,

²⁴³ al-Nadawī, *Mawsū‘ah al-Qawā‘id wa al-Ḍawwābiṭ al-Fiqhiyyah al-Ḥākimah lil-Mu‘āmalāat al-Māliyah*, 1, p138.

²⁴⁴ See: al-Saati, "The Permissible Gharar (Risk) in Classical Islamic Jurisprudence "; al-Darir, *Al-Gharar in contracts and its effects on contemporary transactions*.

²⁴⁵ See: Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu‘āmalāt al-Māliyyah*, p40; Rosman, "al-Ḥiyal wa al-Makhārīj fī al-Mu‘āmalāt al-Maṣrifīyyah al-Islāmiyyah," p79; Muḥammad Abū Zahrah, *Abū Ḥanīfah Ḥaātuh wa ‘Aṣruh Arā‘uh wa Fiqhuh* (Dār al-Fikr al-‘Arabī, 1991), p379.

²⁴⁶ See: Muḥammad al-Khiḍr Ḥsayn, *al-Sharī‘ah ṣāliḥh lilul Zamān wa Makān*, ed. Muḥammad ‘Imārah (Naḥḍah Maṣr, 1999); Yūsuf al-Qarḍāwī, *Sharī‘ah al-Islām Ṣāliḥh lil-Taṭbīq fī Kul Zamān w Makān*, 2ed ed. (Dār al-Ṣaḥwah, 1993).

²⁴⁷ On the argument that an interest-free economy is in fact feasible, see Arshad Zaman and Asad Zaman, "Interest and the Modern Economy," *Islamic Economic Studies* 8, no. 2 (2001).

and Ḥanbalī schools, which have the greatest impact on contemporary Islamic finance. It also addresses the position of other schools which have less impact on the industry but could play an active role in the future.

Generally, early jurists and founders of schools did not directly state their position on *ḥīlah*, but a theory about their view can be formed by examining their ruling on different contracts.²⁴⁸ Later jurists have tried to articulate the general principles of some of these schools and their founders on this issue.²⁴⁹ However, as with every general rule, some exceptions exist where the jurists did not follow the principles of their schools due to certain justifiable reasons²⁵⁰—for example, a prophetic tradition could exempt a transaction from the general prohibition. Such exceptions need to be excluded to form an overall theory.

2.4.1. The Shāfiʿī School

The reason to begin by examining the position of the Shāfiʿī School is that many controversial Shariʿah-compliant products in the industry, particularly in Malaysia, are based on the views of this school.²⁵¹ Shāfiʿī jurists did not directly approve the use of *ḥīlah*, but it can be drawn from their *fatwa* in relation to usury, *shufʿah* (pre-emption), and *waqf* (charitable endowment).²⁵² In particular, their position can be understood from rulings on the validity of four conventional contracts, namely *bayʿ al-ṭinah* transactions, selling grapes to a wine maker, selling weapons during a time of

²⁴⁸ See for example: Abd al-Razzāq al-Sanhūrī, *Maṣādir al-Ḥaq fī al-Fiqh al-Islāmī*, vol. 4 (Cairo: Jāmiʿah al-Duwal al-ʿArabīh 1967), p54; Wahbah al-Zuhaylī, *al-Fiqh al-Islāmī wa Adilatuluh* 4th ed., vol. 4 (Dār al-Fikr, 1997), p3034; al-Qurashī, *Ishkāliyyah al-Ḥiyal fī al-Baḥth al-Fiqhī*, p177.

²⁴⁹ See for example: Aḥmad Ibn Ḥajar al-ʿAsqalānī, *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, ed. Muḥammad Fuʿād ʿAbd al-Bāqī, vol. 12 (Dār al-Maʿrifah, 1963), p328; Ibn al-Qayyim, *Iʿlām al-Mawqīʿ ayn ʿan Rab al-ʿĀlamīn*, 3, p281; Ibn Taymiyah, *Bayān al-Dalīl ʿalā Ibtāl al-Tahlīl*, p134.

²⁵⁰ ʿabd al-Salām al-Ḥiṣayn, *al-Qawāʿid wa al-Ḍawābiḥ al-Fiqhiyah lil-Muʿāmalāt al-Māliyah ʿind Ibn Taymiyah*, vol. 2 (Dār al-Taʿšīl, 2002), p199.

²⁵¹ See: Nagaoka Shinsuke, "Beyond the Theoretical Dichotomy in Islamic Finance: Analytical Reflections on Murābahah Contracts and Islamic Debt Securities," *Kyoto Bulletin of Islamic Area Studies on Islamic Finance* 1, no. 2 (2007): p79; Rosman, "al-Ḥiyal wa al-Makhārīj fī al-Muʿāmalāt al-Maṣrifīyah al-Islāmiyyah," p358.

²⁵² "al-Ḥiyal wa al-Makhārīj fī al-Muʿāmalāt al-Maṣrifīyah al-Islāmiyyah," p103.

disorder, and *nikāḥ al-taḥlīl*, a formalistic contract allowing women to remarry a former husband after three divorces.²⁵³ Al-Shāfi‘ī (d.204/820), the founder of the school, made it clear that the motives of parties to a contract which is valid *ab initio* are immaterial and would not affect the validity of the contract:

The rule I follow is that I do not void any contract which appears valid, because I suspect the intention of the parties or their practice but I validate it based on its form. However, I reprehend the intention which, when made explicit, would void the sale, as I reprehend a person who purchase a sword with intent to use for murder. In this case, the seller is not prohibited from selling the sword to a person he thinks would use it for murder because the buyer might not use it to commit murder. Therefore, I do not void this transaction. Likewise, I reprehend a transaction in which the seller sells grapes to whom he thinks would make wine from it; but I do not invalidate it if he sold it because grapes were permissible at the time of the transaction and the purchaser might not ever use it to make wine; just as the purchaser of the sword might not ever use it to commit murder.²⁵⁴

Furthermore, al-Shāfi‘ī states that a contract can only be invalidated based on the terms explicitly stated in the contract. It is not voided by pre-contract or post-contract arrangements, nor shall it be voided because an illegal motive such as practicing usury is suspected or because it can lead to impermissible action.²⁵⁵ Similarly, al-Nawawy (d.676/1278), an authoritative scholar within the Shāfi‘ī School, asserts this rule: “What matters according to our School, is the form of contract not the intention of the parties; therefore, we validate *‘inah* transaction and *nikāḥ al-taḥlīl*”.²⁵⁶

However, it should be noted that al-Shāfi‘ī’s validation of the form of these contracts does not mean that he considers the use of *ḥīlah* permissible.²⁵⁷ The context of his statement and the evidence which he cites to support his view show that he was

²⁵³ See: Muḥammad Idrīs al-Shāfi‘ī, *al-Umm*, ed. Muḥammad Zuhrī al-Najār, vol. 3 (Mmaktabah al-Kullīāt al-Azhariyah, 1961), p74; Muḥyyī al-Dīn Yaḥyā al-Nawawy, *Rawḍah al-Ṭālibīn wa ‘Umdah al-Muḥtāṭ*, ed. Zuhayr al-Shāwīsh, vol. 3 (al-maktab al-islāmī, 1385), p417; Fathī al-Duranī, *al-Nazariyāt al-Fiqhīyah*, 4th ed. (Jāmi‘ah Dimashq, 1996), p237; al-Sanhūrī, *Maṣādir al-Ḥaq fī al-Fiqh al-Islāmī*, 4, p54; al-Zuhaylī, *al-Fiqh al-Islāmī wa Adilatuh* 4, 3034.

²⁵⁴ al-Shāfi‘ī, *al-Umm*, 3, p74.

²⁵⁵ Ibid. vol 7 p 297

²⁵⁶ Muḥyyī al-Dīn Yaḥyā al-Nawawy, *al-Majmū‘ Sharḥ al-Muhadhdhab*, ed. Muḥammad Najīb al-Muṭī, vol. 9 (Maktabah al-Irshād, 1971), p314.

²⁵⁷ al-Qurashī, *Ishkālīyyah al-Ḥiyāl fī al-Baḥth al-Fiqhī*, p206.

arguing from a judicial perspective. If a dispute on such a contract comes before a judge, it shall be deemed valid from the *al-ḥukm al-waḍ'ī* perspective.²⁵⁸ In the quotation above, al-Shāfi'ī states clearly that the contract would be deemed void if the illegal intention were made explicit. He also states that he regards this intention as reprehensible from the perspective of *al-ḥukm al-taklīfī*. The word *makrūh* which he used can mean “prohibited” or “reprehensible” in the terminology of early jurists.²⁵⁹

Thus we see the Shāfi'ī jurists debate whether the use of *ḥīlah* in the form of these contracts is just reprehensible or actually prohibited, which is the view of the majority of Shāfi'ī jurists.²⁶⁰ Ibn Ḥajar al-'Asqalānī (d.852/1448) seems in favour of the latter.²⁶¹ According to him, whoever intends the collection of usury through the contract of sale is not exempted from sin. Likewise, any means used to circumvent a forbidden matter is prohibited. There is no difference between the prohibition of the illegitimate end and the prohibition of the means that is used to reach the forbidden end.²⁶² In fact, some of the early prominent Shāfi'ī scholars, such as Abū Ishāq al-Isfariyanī (d.418/1027) and Abū Muḥammad al-Juwaynī (d.438/1047), not only prohibit the *īnah* transaction, but also void a sale contract if one of the parties involved makes a habit of using the *īnah* transaction.²⁶³ In addition, many Shāfi'ī jurists state that scholars are forbidden to teach or draw people's attention to such legal ruses to avoid obligation or breach prohibition, and people are prohibited from

²⁵⁸ See generally: Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari'ah in Islamic Banking and Finance," p15.

²⁵⁹ Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3. vol 1 p39al-Qurashī, *Ishkālīyyah al-Ḥiyāl fī al-Baḥth al-Fiqhī*, p208. al-Shāfi'ī himself uses the term in another place in the same book to refer to a prohibited action. See: al-Shāfi'ī, *al-Umm*, 3. vol 5 p 78.

²⁶⁰ al-'Asqalānī, *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, 12, p328; al-'irāqī zan al-Dīn 'abd al-Raḥman, *Ṭarḥ al-Tathrīb fī Sharḥ al-Taqrīb*, ed. Aḥmad 'Abd al-Raḥīm Abū Zar'ah, vol. 2 (Dār Iḥyā' al-Turuāth al-'arabī, 1934), p21; 'abd āl-Raḥman Muḥammad Bā'alawī, *Bughyah al-Mustarshidīn* (Dār al-Fikr, 2001), p127. Ibn Bayyah, a renowned contemporary scholar, argues that validating prohibited contracts contradicts the principles of al-Shāfi'ī. See Ibn Bayyah, *Sadd al-Dharī'ah wa Taṭṭībqātuh fī Majāl al-Mu'āmalāt*, p66.

²⁶¹ al-'Asqalānī, *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, 12, p328.

²⁶² Ibid.

²⁶³ al-Nawawy, *Rawḍah al-Tālibīn wa 'Umdah al-Mufīn*, 3, p417.

asking a *fatwa* from whomever has been known to do so.²⁶⁴ As al-‘Asqalānī does, Abū Ḥātim al-Quzwīnī (d.440/1048), the author of the only surviving Shāfi‘ī book on *hīlah*, states a clear difference between prohibited *hīlah* and permissible *hīlah*.²⁶⁵

This understanding of the Shāfi‘ī School position is further supported by al-Shāfi‘ī’s view on other *ribā*-related cases. Ibn al-Qayyim points out that al-Shāfi‘ī prohibits an exchange related to *ribā al-faḍal*²⁶⁶ known as *mudd ‘ajwah*, where two *ribawī* items are exchanged and one of them includes an additional item of a different sort—for example, the exchange of one kilo of dates and five grams of silver for two kilos of dates.²⁶⁷ This transaction, according to al-Shāfi‘ī, is not permissible and is seen as a way of breaching the prohibition of *ribā al-faḍal*. Similarly, Ibn al-Qayyim argues that some *hīlah*-related transactions that are validated by the Shāfi‘ī School are more worthy of prohibition because they lead to breaching of *ribā al-nasī’ah* (the usury of delay), which, unlike the transaction in question (*mudd ‘ajwah*), is unanimously prohibited.²⁶⁸ Moreover, Ibrāhīm notes that although al-Shāfi‘ī validates ‘*inah* transactions, he voids other types of *hīlah* related to *al-kirā’* (lease) and *al-qirāḍ* (silent partnership).²⁶⁹ In short, the Shāfi‘ī School’s position on *hīlah* is that even though some instances of it are deemed legally valid, using it to achieve unlawful ends is prohibited.

²⁶⁴ *al-Majmū‘ Sharḥ al-Muhadhdhab*, 9. vol 1 p⁴ Bā‘alawī, *Bughyah al-Mustarshidīn*, p10.

²⁶⁵ Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu‘āmalāt al-Māliyyah*, p76.

²⁶⁶ Literally “the usury of surplus.” Such sales involve an excess or delay in exchange of certain types of goods (*ribawī*) that all fall within a single category. See: Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p302.

²⁶⁷ See: al-Shāfi‘ī, *al-‘Umrānī, Yahyā*, 5, p196.

²⁶⁸ Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p188.

²⁶⁹ *Al-qirāḍ* or *muḍārabah* is a type of partnership where one partner provides the capital (*rab al-māl*) to another partner (*muḍārib*) who manages the investment. See El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p120.

2.4.2. *The Ḥanafī School*

The Ḥanafī School generally takes a similar position to the Shāfi'ī School in disregarding parties' motives behind contracts.²⁷⁰ Its founder Abū Ḥanīfah validates the selling of grapes to a winemaker and hiring Muslims to carry wine, as well as the contract of *nikāḥ al-tahlīla* and selling materials which can be used to make weapons at a time of disorder.²⁷¹ In addition, books containing practises of valid *ḥīlah* are attributed to scholars within the Ḥanafī School, such as Muḥammad Ibn al-Ḥasan al-Shaybāny (d.189/805)²⁷² and Abū Bakr al-Khaṣṣāf (d. 261/874).²⁷³

However, the validation of some *ḥīlah* does not necessarily imply its permissibility, according to the Ḥanafī School. Many jurists within the school, including Abū Ḥanīfah, al-Shaybāny, and al-Khaṣṣāf, have made it clear that *ḥīlah* becomes prohibited when it is misused to harm or deny other people's rights.²⁷⁴ Such an understanding also seems clear to late Ḥanafī scholars, as attested in the book of *al-Fatāwā al-Hindiyah*: "The view of our scholars is to prohibit any *ḥīlah* used by a person to void others' rights or to make people suspect it as well as disguising what it is null and void".²⁷⁵

Like Abū Ḥanīfah, al-Shaybāny, one of most authoritative jurists in the Ḥanafī School, prohibits the *'īnah* transaction and sees it as being invented by the consumers of usury. He describes the burden of evil of engaging in such transaction as being as

²⁷⁰ al-Sanhūrī, *Maṣādir al-Ḥaq fī al-Fiqh al-Islāmī*, 4, p56; al-Duranī, *al-Nazarīyāt al-Fiqhīh*, p233.

²⁷¹ See: Ibn 'ābidīn, *Raddu al-Muḥtār 'Alā al-Durri al-Mukhtār sharḥ Tanwīr al-Abṣār*, 4, p268; al-Zuhaylī, *al-Fiqh al-Islāmī wa Adīlatuh* 4, p3033.

²⁷² Muḥammad Ibn al-Ḥasan al-Shaybāny, *al-Makhārij fī al-Ḥiyal* (Maktabah al-Thaqāfah al-Dīnīh, 1999).. Some researchers dispute the authenticity this book's attribution to al-Shaybāny; see: Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu'āmalāt al-Māliyyah*, p27; Rosman, "al-Ḥiyal wa al-Makhārij fī al-Mu'āmalāt al-Maṣrifīyyah al-Islāmiyyah," p6; al-Qurashī, *Ishkālīyyh al-Ḥiyal fī al-Baḥth al-Fiqhī*, p158; Aḥmad Muḥammad al-Naqīb, *al-Madhhab al-Ḥanafī*, vol. 1 (Maktabah al-Rushd, 2001), p413.

²⁷³ See: Schacht, *An Introduction to Islamic Law*, p81.

²⁷⁴ See: al-'Asqalānī, *Fatḥ al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, 12, p331; al-Khaṣṣāf, *Kitāb al-Ḥiyal*, 5; al-Shātibī, *al-Muwāfaqāt*, 1. Vol 5, p188.

²⁷⁵ Niẓām al-Dīn al-Balkhī and Others, *al-Fatāwā al-Hindiyah fī Madhhab al-Imām al-A'zam abī Ḥanīfah al-Nu'mān*, vol. 6 (Dār al-Fikir, 1991), p390.

heavy as mountains.²⁷⁶ Similarly, Abū Yūsuf (d.182/798), another authoritative scholar who was a student of Abū Ḥanīfah and the Chief Justice in his time, wrote about the prohibition against using *ḥīlah* to avoid the payment of obligatory tax in his renowned book *al-Kharāj (Treatise on Taxation)*, which he authored at the caliph's request. The text reads:

It is not permissible for a person who believes in Allah and the day of judgment to not pay the *ṣadaqah* (obligatory charity tax), or to split his property or divide it by a formalistic sale or any kind of legal tricks to avoid the payment of *ṣadaqah*.²⁷⁷

Furthermore, the position of the Ḥanafī School appears clear to other schools of thought. For instance, Ibn Ḥajar of the Shāfi'ī School states,

The advocating of *ḥīlah* has been widely attributed to Ḥanafī School because Abū Yūsuf has authored a book on the subject. However, their jurists are known to limit its implementation to what is right".²⁷⁸

In fact, al-Qurashī argues that there is a very strong voice—at least theoretically—within the Ḥanafī School supporting substance over form.²⁷⁹ However, although such a position suits their heavy reliance on *qyās* (analogy) as a source of Shari'ah, he later admits that it might not be the case in practise.²⁸⁰ Similarly, Hassan argues that the Ḥanafī School considers intention where indications of intent can be drawn from the circumstances and norms surrounding the action.²⁸¹ He cites the example of pronouncing a divorce at the time of death-sickness (*marāḍ al-mawt*); while the Shāfi'ī School completely validates such a divorce and excludes the wife from inheritance, the Ḥanafī allow the wife to inherit her share according to Shari'ah inheritance law as long as she is still in the *iddah* (a legal waiting period before the

²⁷⁶ Ibn 'ābidīn, *Raddu al-Muhtār 'Alā al-Durri al-Mukhtār sharḥ Tanwīr al-Abṣār*, 4., vol 5 p273.

²⁷⁷ Abū Yūsuf, *Kitāb al-Kharāj*, p80.

²⁷⁸ al-'Asqalānī, *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, 12, p326. See also: al-Shāṭibī v1o5, p188.

²⁷⁹ al-Qurashī, *Ishkāliyyah al-Ḥiyāl fī al-Baḥth al-Fiqhī*, p169.

²⁸⁰ Ibid.

²⁸¹ Hussain Hamed Hassan, *Nazarīh al-Maṣlahah f al-Fiqh al-Islāmī* (Maktabah al-Mutanabī, 1981), p295.

women can remarry). The rationale for such a ruling is that the husband, by divorcing his wife after the illness that is likely to cause his death, is seen as trying to circumvent the Shari‘ah inheritance law. However, unlike the Mālikī and Ḥanbalī schools of thought, Ḥanafī does not extend such a ruling after the passing of *‘iddah* time. Thus, this case is an exception to the school’s general theory on disregarding intention from a validity perspective, and it is not sufficient to support the argument of Hassan.²⁸²

Nonetheless, it is important not to accept the outright characterisation of the Ḥanafī School as pro-*ḥīlah*. The authenticity of such a claim must be cross-checked with the view stated in the authoritative books of the school, rather than in history and biography books.²⁸³ In addition, the isolated opinions or practises of a few individual scholars should not be attributed to the whole school.²⁸⁴ Ibn Taymiyah and Ibn al-Qayyim point out that numerous *ḥīyal* invented by jurists from different schools of thought contradict the principles of the founders of these schools.²⁸⁵ Ibn Baṭāh al-‘Ukbarī (d.387/997) narrates a story in which he asks a respected Shāfi‘ī jurist about a *ḥīlah* that was attributed to al-Shāfi‘ī. The scholar is surprised about this claim and cites Abū ‘Abdi Allāh al-Zubayrī (d.306/929), an authoritative scholar within the Shāfi‘ī *madhhab*, who firmly denounces the existence of such opinion of al-Shāfi‘ī.²⁸⁶ Even within the Mālikī and Ḥanbalī Schools, where the positions of Mālik Ibn Anas and Aḥmad Ibn Ḥanbal, the school founders, are very strict against *ḥīlah*, such a practise has been recorded. According to Ibn Taymiyah, some of the Ḥanbalī scholars

²⁸² For the position of different schools on pronouncing divorce at the time of death-sickness, see: Wzārah al-Awqāf al-Kuwaytīyah, *al-Mawsū‘ah al-Fiqhiyyah*, vol. 32 (Wzārah al-Awqāf al-Kuwaytīyah, 1995), p75; Hassan, *Naẓarīh al-Maṣlahah f al-Fiqh al-Islāmī*, p295.

²⁸³ al-Qurashī, *Ishkāliyyah al-Ḥīyal fī al-Baḥth al-Fiqhī*, p161.

²⁸⁴ Ibid., p88; Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p130.

²⁸⁵ *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p134; Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p281.

²⁸⁶ Ibn Baṭāh al-‘Ukbarī, *Ibtāl al-Ḥīyal*, ed. Sulaymān al-‘Umayr (Al-Resalah 1996), p144.

went as far as using *hīlah* to legalise specific cases that were explicitly prohibited by Ibn Ḥanbal himself.²⁸⁷

Besides, many *hīyal* validated by late Ḥanafī and Shāfi'ī scholars were based on individual cases that do not necessarily correspond to the original ruling of the schools' founders.²⁸⁸ This process is called *takhrīj*, where in the absence of an opinion from the founding scholars on the case in question, a jurist would derive an opinion from a ruling of the school's founder on a different case, or the jurist would use his legal methodology to derive an opinion from the original sources of Shari'ah.²⁸⁹ However, in some cases, according to Ibn al-Qayyim,²⁹⁰ the follower jurists extended the ruling beyond what the school's founder had originally authorised and attributed it to him. He argues that some of these *hīyal* cannot possibly be allowed by the founding scholars, taking into account their religious piety and the general principles of the school.²⁹¹ In summary, the position of the Ḥanafī School is generally similar to the Shāfi'ī School view: although it validates some *hīyal* from the perspective of *al-ḥukm al-waḍ'ī*, the misuse of *hīlah* to achieve illegal ends is prohibited from an *al-ḥukm al-taklīfī* perspective.

2.4.3. *The Mālikī School*

According to the Mālikī School, the use of *hīlah* is prohibited and it invalidates contracts.²⁹² Al-Shāṭibī, a Mālikī scholar, has written extensively on the subject.²⁹³ In

²⁸⁷ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p134. . See also: al-'Ukbarī, *Ibtāl al-Ḥiyal*, p143.

²⁸⁸ See: Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p130; Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p281; al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī*, p88; Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu'āmalāt al-Māliyyah*, p31.

²⁸⁹ Wael B. Hallaq, *The Origins and Evolution of Islamic Law* (Cambridge, UK: Cambridge University Press, 2005), p161. For an extensive study of *takhrīj* see: Ya'qūb 'Abd al-Wahāb al-Bāḥsayn, *al-Takhrīj 'ind al-Fuqahā' w al-Aṣūliān* (Maktabah al-Rushd, 1994).

²⁹⁰ Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p281.

²⁹¹ Ibid.

²⁹² Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p31; Rosman, "al-Ḥiyal wa al-Makhārij fī al-Mu'āmalāt al-Maṣrifīyyah al-Islāmiyyah," p123; Coulson, *A History of Islamic Law*, p141; al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī*, p331; Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu'āmalāt al-Māliyyah*, p30.

fact, the Mālikī school has been criticised for applying the principles of *sad al-dhariā`i*²⁹⁴ (precautionary legal prohibition) to ban many contracts on the basis that they may lead to unlawful ends.²⁹⁵ For example, *ṭnah*, *al-tawarrq*, and some forms of *murābahah*²⁹⁶ contracts are deemed prohibited by the Mālikī school of thought.²⁹⁷

2.4.4. The Ḥanbalī School

Similarly, the Ḥanbalī School strongly forbids the use of *ḥīlah* and deems it void.²⁹⁸ Aḥmad Ibn Ḥanbal,²⁹⁹ the school's founder, characterises the people who use *ḥīlah* as malicious.³⁰⁰ Many of the classical works of literature opposing the use of legal ruse were written by Ḥanbalī jurists. For example, Ibn Baṭāh al-ʿUkbarī³⁰¹ dedicated a book to the subject titled *Ibtāl al-ḥiyal* (*The Voiding of Legal Ruses*). He describes those who advise how to circumvent the teaching of Shariʿah as hypocrites who should not be called scholars. He argues that by trying to deceive Allah, one only deceives himself, as Allah knows the true intention behind any actions.³⁰² However, two Ḥanbalī scholars have taken the lead in the battle against *ḥīlah*: Ibn Taymiyah on

²⁹³ See: al-Shāṭibī, *al-Muwāfaqāt*, 1, p124; Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*, p173.

²⁹⁴ Literally, “the blocking of means”; the blocking of actions that could lead to unlawful ends. See: Kamali, *Principles of Islamic Jurisprudence*, p397.

²⁹⁵ See: Ibn Bayyah, *Sadd al-Dharīʿah wa Taṭṭbīqātuh fī Majāl al-Muʿāmalāt*, p48; Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p240; Ibn Taymiyah, *al-Qawāʿid al-Nawrānīh al-Fiqhiyah*, p119.

²⁹⁶ *Al-tawarrq* and *murābahah* are two common methods used to structure Islamic financial services. The two methods have various definitions and applications. For further information, see chapter 1 p30 and chapter 3 p74.

²⁹⁷ al-Qurashī, *Ishkāliyyh al-Ḥiyal fī al-Baḥth al-Fiqhī*, p344.

²⁹⁸ Ibn Taymiyah, *Bayān al-Dalīl ʿalā Ibtāl al-Taḥlīl*, p31; Rosman, "al-Ḥiyal wa al-Makhārij fī al-Muʿāmalāt al-Maṣrifīyyah al-Islāmiyyah," p123; Coulson, *A History of Islamic Law*, p141; al-Qurashī, *Ishkāliyyh al-Ḥiyal fī al-Baḥth al-Fiqhī*, p363; Ibn Taymiyah, *al-Qawāʿid al-Nawrānīh al-Fiqhiyah*, p118.

²⁹⁹ See *Majmūʿ Fatāwā Shaykh al-Islām Ibn Taymiyah*, ed. Abd al-Raḥman Ibn Qāsim, vol. 20 (Mujammaʿ al-Malik Fahd liṭibāʿat al-Muṣḥaf al-Sharīf, 2004), p230.

³⁰⁰ al-ʿUkbarī, *Ibtāl al-Ḥiyal*, p120.

³⁰¹ *Ibid.*, p94,108. The editor mentions other books written by Ḥanbalī scholars on the subject; see p42.

³⁰² *Ibid.*

the contract of *nikāḥ al-tahlīla*, and later his student Ibn al-Qayyim.³⁰³ Most of the contemporary literature on *ḥīlah* is based on their work.

2.4.5. *Other Schools of Thought*

Although the primary aim of this chapter is to investigate the position of the major *sunni* Islamic schools of thought which have the most impact on contemporary Islamic finance, it is worth exploring the positions of other schools of thought that may play a future role in the Islamic finance industry.

The *Zāhirī* School is not widely followed at the present time.³⁰⁴ However, because some of its views are cited in the classical and contemporary literature on comparative jurisprudence, it is worth addressing its treatment of *ḥīlah*. The *Zāhirī* School does not directly support *ḥīlah*, but due to its literalist approach, it has taken the same position of pro-*ḥīlah* schools on some of the jurisprudential issues³⁰⁵ such as the *ʿīnah* transaction and *nikāḥ al-tahlīla*.³⁰⁶ For instance, on the issue of the *ʿīnah* transaction, Ibn Ḥazm strongly defends its lawfulness, basing his argument on the general permissibility of sale, which is stated in Quranic verse, “Allah has permitted trade”. In fact, he goes as far as arguing that parties should not be blamed even if their intention was to collect interest through an *ʿīnah* transaction; rather, they should be rewarded, as they used two legitimate transactions rather than one usurious transaction to achieve their end! In his view, those who invalidated the sale are the ones to be

³⁰³ See: Ibn al-Qayyim, *Iʿlām al-Mawqīʿayn ʿan Rab al-ʿĀlamīn*, 3; Ibn Taymiyah, *Bayān al-Dalīl ʿalā Ibtāl al-Taḥlīl*; Ibn Bayyah, *Sadd al-Dharīʿah wa Taṭṭbīqātuh fī Majāl al-Muʿāmalāt*, p39; Ibrāhīm, *al-Ḥiyāl al-Fiqhiyyah fī al-Muʿāmalāt al-Māliyyah*, p32; Schacht, *An Introduction to Islamic Law*, p81; Coulson, *A History of Islamic Law*, p141.

³⁰⁴ For more about *Zāhirī* School see: Ignaz Goldziher, *The Zahiris: Their Doctrine and Their History*, ed. Wolfgang Behn, trans. Wolfgang Behn (Leiden; Boston: Brill, 2008); Abdel-Magid Turki, “al-*Zāhiriyya*,” in *Encyclopaedia of Islam*, ed. P. Bearman, et al. (Brill Online, 2012) <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/al-zahiriyya-SIM_8086> accessed 30 April 2012

³⁰⁵ Ibrāhīm, *al-Ḥiyāl al-Fiqhiyyah fī al-Muʿāmalāt al-Māliyyah*, p30.

³⁰⁶ See: ʿAlī Aḥmad Ibn Ḥazm, *al-Muḥallā bi-al-ʿĀthār*, ed. ʿAbd al-Ghaffār Sulaymān al-Bnadārī, vol. 7 (Dār al-Fikr, 1988), p554.; also vol 12, p195.

blamed for mistrusting the intention of people and accusing them of using *ḥīlah* to commit the prohibited.

However, it is notable that Ibn Ḥazm validates *īnah* transaction and *nikāḥ al-taḥlīla* not because he legalises the use of *ḥīlah*, but rather because the literal approach which he follows does not prohibit these contracts. Hence, other contracts allowed by pro-*ḥīlah* schools are deemed prohibited under the Zāhirī School. For example, while Abū Ḥanīfah permits the selling of grapes to a wine maker, Ibn Ḥazm considers it a forbidden and void transaction.³⁰⁷ In fact, on another issue related to punishment of adultery, he attacks the view of Abū Ḥanīfah and states that the Ḥanafī view on this issue and on other jurisprudential matters has taught people how to use *ḥīlah* to avoid punishment.³⁰⁸ In short, the inconsistency of the Zāhirī position towards *ḥīlah* is due to its literal method, which rejects other schools' use of analogy and does not extend the objectives of the law beyond those explicitly stated in the letter of the law.³⁰⁹

The *shī'ī imāmīh* school of thought, which is active in Iran, Iraq, and Bahrain,³¹⁰ generally prohibits the use of *ḥīlah*, though some of it is deemed legally enforceable.³¹¹ The Zaydiyyah school of thought, which has spread in Yemen, has a position very close to that of the *sunni* schools which are against *ḥīlah*, such as the

³⁰⁷ Ibid., p522. p522.

³⁰⁸ Ibid., 12: p196. Vol 12, p196

³⁰⁹ See: Goldziher, *The Zahiris: Their Doctrine and Their History*, p42. Goldziher gives an example of the Zāhirī position on the law of usury, noting that "The Zāhirite school . . . views such syllogism as an arbitrary notion which is falsely and arbitrarily attributed to the purpose of the legislator. It delimits the law exclusively to the personal or non-personal cases enumerated in the law. According to the view of the Zāhirite school, one must not search for the cause of any of God's laws, just as the cause for the creation of any of God's works must not be investigated. The only cause for their creation is God's sovereign will; exactly the same applies to law."

³¹⁰ It is worth pointing out that in Bahrain, some Shari'ah supervisory boards consist of *sunni* and *shī'ī* scholars. See: Quṭb al-'Arabī, "al-Bahrayn al-Maṣārif al-Islāmiyah Tūḥḥad al-Shī'ah wā al-sunnah," Alarabiya.Net, <http://www.al-asfoor.org/?id=1002>. accessed 10 April 2012

³¹¹ See: al-Muḥaqq al-Ḥilī, *Sharā'ī al-Islām fī Masā'il al-Ḥalāl wa al-Ḥarām*, ed. al-Sayyid ṣādiq al-Shīrāzī, vol. 3 (Intishārāt Istiql-āal, 1983), p596; Yūsuf al-Baḥrānī, *al-Ḥadā'iq al-Nāḍirah fī Aḥkām al-Utrah al-Ṭāhirah*, ed. Muḥammad Taqī al-Ayrawānī, 2ed ed., vol. 25 (Dār al-Aḍwā', 1989), p375; al-Mīlānī, "al-Iftirād al-Qānūnī wa al-Ḥīlah al-Shar'īyyah".

Mālikī and Ḥanbalī Schools.³¹² It explicitly invalidates *‘īnah* transactions and other *ḥīlah* that are used to circumvent the prohibition of *ribā*.³¹³ al-‘Anasy (d.1390/1970), an authoritative Zaydī jurist, states, “According to our school, the hidden motive in *ribā*-related contracts is considered as if it is stated. Therefore, such a contract is invalid, as well as any other *ḥīlah*”.³¹⁴ Similarly, the literature of the *ibāḍī* school, which is dominant in Oman, where Islamic finance was recently introduced,³¹⁵ shows a strong position against *ḥīlah*.³¹⁶

Contemporary Shari‘ah supervisors seem to be in favour of supporting substance over form in principle. al-Ḥaddād³¹⁷ cites many examples of Shari‘ah supervisory board *fatwas* which include conditions aiming to avoid sham contracts. However, in practise, he argues that such provisions are not taken into consideration and they are hardly applied.

In some cases, different schools debate over certain contracts not because one party is supporting form over substance, but because they dispute whether it contradicts with the objectives of Shari‘ah or not. This explains why a few *ḥīlah* have been accepted by the Mālikī and Ḥanbalī schools, although their position is very strict against it.³¹⁸ For example, Ḥanbalī deems the contract of *nikāḥ al-taḥlīla* a legal ruse which circumvents the prohibition of remarrying a former husband after triple

³¹² See: Aḥmad Yaḥyā al-Murtadā, *al-Baḥr al-Zakhār al-Jāmi‘ Limadhdhāhib ‘Ulamā’ al-Amṣār*, vol. 3 (Dār al-Kitāb al-Islāmī, 1973), p187.

³¹³ Ibid. vol 4 p387, vol 5p23, Aḥmad Qāsim al-‘Anasy, *al-Tāj al-Mudhdhab l’Aḥkām al-Madhab*, vol. 2 (Maktabah al-Yaman, 1961), p389.

³¹⁴ *al-Tāj al-Mudhdhab l’Aḥkām al-Madhab*, 2, p390.

³¹⁵ Inesh Nair and Saleh al-Shaibany, "Oman Opens Door to Islamic Banks to curb Fund Outflows," Reuters, <http://uk.reuters.com/article/2011/05/03/oman-banks-idUKLDE7420I720110503?feedType=RSS&feedName=rbssFinancialServicesAndRealEstateNews>. accessed 30 April 2012

³¹⁶ Muḥammad Yūsuf Aṭfaysh, *Sharḥ al-Nīl wa Shifā’ al-‘Alīl*, vol. 8 (Maktabah al-Irshād, 1985), p71., p684, vol 9p25, vol 11p379, vol 17p341

³¹⁷ al-Ḥaddād, "Ma‘āyir al-Tamīz ban al-‘Uqūd al-Ṣūriyyih wa al-Ḥaḥiqiyiyah," p23.

³¹⁸ al-Maṣrī and al-Būṭī discuss Ibn al-Qayyim’s approval of *ḥīlah* that is seen as in conflict with Shari‘ah. See: al-Būṭī, *Dawābiḥ al-Maṣlahah fī al-Sharī‘ah al-Islāmiyyah*, p323; al-Maṣrī, "al-Ḥīl al-Fiḥiyah bayn al-Būṭī wā Ibn Qaim al-Jawziyyah" p45.

divorces, and which conflicts with the objective of the prohibition, namely, restricting husbands' freedom to divorce wives to make them take the matter more seriously. In contrast, the Mālikī School validates the contract on the ground that it allows the reunion of the family and protects the interest of children of the divorced couple, which Shari'ah encourages.³¹⁹ In this example, each school has a different take on the objective of the law. This might offer an explanation to the question raised by some researchers over the inconsistency of some schools towards *ḥīlah*.³²⁰

In summary, from a permissibility point of view (*al-ḥukm al-taklīfī*), there is generally no authority for employing a form to circumvent the spirit of Islamic finance, as the position of different schools of thought shows. However, from a judicial validity perspective (*al-ḥukm al-waḍ'ī*), if such a form has been used, it can be deemed valid according to some schools of thought, such as Shāfi'ī and Ḥanafī.

2.5. Refuting the Pro-*Ḥīlah* Arguments

Several arguments have been put forward for and against the validity of *ḥīlah*. The legal question is whether the validity of a contract should be based on its external structure regardless of motives behind it, or whether it should be deemed void due to any suspected unlawful motives.³²¹ As appropriate to the purposes of this thesis, this section will only examine arguments directed at the use of *ḥīlah* within Islamic finance. It will not discuss any cases which both parties agree fall into the category of permissible *ḥīlah* (*makhraj fiqhī*) or prohibited *ḥīlah*.

The view of validating a *ḥīlah* contract in the judicial context is based on several prophetic traditions and rational justifications. First, proponents argue that motive

³¹⁹ Ibrāhīm Mūsā al-Shātibī, *al-Muwāfaqāt*, ed. Mashhūr Ḥasan Salmān, vol. 3 (Dār Ibn 'Affān, 1997), p125; Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*, p185.

³²⁰ See for example: Schacht, "Ḥiyāl."; Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*, p185.

³²¹ Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p233.

falls outside the essentials requirement of a contract; as long as the form of the transaction was concluded according to the free will of the parties and with no explicit illegitimate conditions, intention should not affect its legal enforceability.³²² Investigating motives behind contract is beyond the powers of the judge, as only Allah can judge a person's intentions. Therefore, a judge can base his judgment only on the visible action.³²³ Al-Shāfi'ī goes further to argue that this was the norm for Prophet Muhammad, and cites the *ḥadīth* where the Prophet states,

I am only a human being, and you people have disputes. May be someone amongst you can present his case in a more eloquent and convincing manner than the other, and I give my judgment in his favour according to what I hear. Beware! If ever I give (by error) somebody something of his brother's right then he should not take it as I have only, given him a piece of Fire.³²⁴

Ibn Taymiyah³²⁵ accepts that intention is irrelevant to the validity of a contract when there are no evidentiary indications of it; however, he argues that if the parties' actions and the circumstances surrounding the contract inform us that the substance of the contract differs from its form, then intention becomes relevant. Accordingly, taking into consideration this circumstantial evidence is not merely judging intention, but rather judging the appearance of actions. He argues that it is insensible, for example, to assume that a person who is well-known for conducting the contract of *nikāḥ al-taḥlīla* or for using *ḥīlah*-related transactions to collect usury actually intends a real marriage or an actual trade every time.³²⁶ Following Ibn Taymiyah's logic, it is similarly difficult to assume that when financial institutions which mainly

³²² al-Shāfi'ī, *al-Umm*, 3. vol 7 p 297

³²³ Ibid. vol 4 p114; Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p234.

³²⁴ Muhammad Ismā'īl al-Bukhārī, "Ṣaḥīḥ al-Bukhārī," Sunnah.com, <http://sunnah.com/urn/65530>. accessed 1 April 2012, vol. 9, Book 86, *Ḥadīth* 97

³²⁵ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p282.. See also Paul R. Powers, *Intent in Islamic Law : Motive and Meaning in Medieval Sunni Fiqh* (Leiden; Boston: Brill, 2006), p117-18.

³²⁶ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p282. See also Powers, *Intent in Islamic Law : Motive and Meaning in Medieval Sunni Fiqh*, p117-18.

lend money at interest offer *ḥīlah*-based Shari‘ah-compliant products, those products are not intended to circumvent the prohibition of usury.³²⁷

In addition, every legal systems ban certain motives that affect the validity of contracts to protect the welfare of the public.³²⁸ For instance, contracting a criminal to commit a crime is void, although it fulfils the basic requirement of a contract. The freedom of contract can be limited when the purpose of undertaking the contracts is illegal.³²⁹

With regard to the argument that Allah is the only one who can judge the intention of a person, al-Shāfi‘ī seems to indicate that *qarā’īn* (indirect evidence) is inadmissible if it can be concluded from the circumstances surrounding the contract but it is not part of the contract.³³⁰ However, as stated by Ibn al-Qayyim,³³¹ most scholars accept this sort of evidence in their judgment. The *ḥadīth* cited in al-Shāfi‘ī’s argument “I base my judgment according to what I hear” does not reject the acceptance of indirect evidence. The *ḥadīth* shows that a judge would consider all the evidence (direct and indirect) represented before him by the parties prior to issuing his judgments. In addition, the *ḥadīth* is more of a moral appeal to the conscience of the winning parties not to take what is not their right.³³²

Another important argument of those who support the validation of *ḥīlah* is that the Prophet authorises the use of a legal ruse to avoid *ribā al-faḍal*, as the following *ḥadīth* shows:

Narrated Abu Said al-Khudri: Once Bilal brought Barni [i.e., a kind of dates] to the Prophet and the Prophet asked him, “From where have you brought

³²⁷ See: al-Qurashī, *Ishkālīyyh al-Hiyal fī al-Baḥth al-Fiqhī*, p267.

³²⁸ Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p235.

³²⁹ Ibid.

³³⁰ Ibid., p236.

³³¹ See: Muḥammad Ibn Abī Bakr Ibn al-Qayyim, *al-Turuq al-Hukmiyyah fī al-Siyāsīh al-Shar‘iyah*, ed. Nāyif al-Ḥamad (Dār ‘ālam al-Fawā’id, 2007); ‘abdAllāh al-‘Ajlāan, *al-Qaḍā’ bi-al-Qarā’in al-Mu‘āṣirh* (Jāmi‘ah al-Imam Moḥammad bin Saud al-Islamiyah, 2006).

³³² Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p237.

these?" Bilal replied, "I had some inferior type of dates and exchanged two $\text{ṣā}'s$ ³³³ of it for one $\text{ṣā}'$ of Barni dates in order to give it to the Prophet to eat". Thereupon the Prophet said, "Beware! Beware! This is definitely Riba [usury]! This is definitely Riba! Don't do so, but if you want to buy [a superior kind of dates] sell the inferior dates for money and then buy the superior kind of dates with that money."³³⁴

This tradition shows that the Prophet asked Bilal not to exchange the bad dates with the good dates directly, but rather asked him to sell the bad dates first for money, and then use it to buy good dates. Initially, acquiring money was unintended, but it was used as a means to achieve the desirable end, which was to obtain the good dates. Therefore, according to this view, the use of *ḥīlah* should be accepted.³³⁵

This argument is valid assuming that the Prophet's instruction to Bilal contradicts the objective of the lawgiver. However, this is not the case, because allowing the exchange of bad dates with good dates directly results in one party being disadvantaged; a trade at any ratio that departs from the market ratio would inevitably lead to this situation.³³⁶ Therefore, the instructions in the *ḥadīth* directed Bilal to sell the first kind of date at the highest possible market price and then to purchase the other kind at the lowest available market price. Ultimately, efficiency in exchange is achieved by making the ratio of marginal utilities equal to the market price ratio.³³⁷

On the other hand, the argument against *ḥīlah* is based on several Quranic verses and Prophetic *ḥadīth*. The Quran refers to the story of some Jews who tried to circumvent the prohibition against fishing on the Sabbath (Saturday). On Friday, they

³³³ A measure for grain used by the people of Medina, equivalent to 2.35 kilograms. See: 'abdAllāh Maṣūir al-Ghufaylī, "al-Ṣā' bayn al-Maqāyīs al-Qadīmah w al-Ḥadīthah," Ṣayd al-Fawā'id, <http://www.saaaid.net/bahoth/80.htm>. accessed 1 May 2012.

³³⁴ al-Bukhārī, "Ṣaḥīḥ al-Bukhārī", Vol. 3, Book 38, Hadith 506

³³⁵ See: al-Būfī, *Ḍawābiḥ al-Maṣlaḥah fī al-Sharī'ah al-Islāmiyyah*, p305; Ibrāhīm, *al-Ḥiyal al-Fiḥriyyah fī al-Mu'āmalāt al-Māliyyah*, p83.

³³⁶ El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p53.

³³⁷ Ibid. Ibn Rushd (Averroes) has pointed out this theory; see: Abu al-Walīd Muḥammad Ibn Rushd, *Bidāyah al-Mujtahid w Nihāyah al-Muqtaṣid* ed. Abd Allāh al-'Abādī, vol. 3 (Dār al-Salāam, 1995), p1375. Vogel and Hayes, *Islamic Law and Finance: Religion, Risk, and Return*, p78; ibid.

would dig ditches which could hold the fish until they could be caught on Sunday.³³⁸

The verse reads:

And ask them about the town that was by the sea—when they transgressed in [the matter of] the Sabbath—when their fish came to them openly on their Sabbath day, and the day they had no Sabbath they did not come to them. Thus did we give them trial because they were defiantly disobedient.³³⁹

Ibn Taymiyah³⁴⁰ points out that the Jews were punished although they did not directly breach the prohibition against fishing on Saturday, but complied with the letter of the law. He argues that the legal ruses used to legalise the collection of usury are worse than the tricks used by those people.³⁴¹

Ibn Taymiyah³⁴² cites another incident in the Quran to support his argument. The Quran records the story of the people of the garden, where the poor used to have the right of picking up what falls from the trees if they plucked the fruits during the daytime. However, when the owners vowed to cut the trees' fruit at night so the poor would not be able to pick anything, an affliction sent by Allah came upon the garden while they were asleep, and it was as if the garden were wrested away.³⁴³ This is a warning for anyone who uses *hīlah* to violate Allah commands or people's rights.³⁴⁴

Furthermore, supporters of the invalidation of *hīlah* record many incidents in which the Prophet warns his companions against the use of deceitful artifices. In one ḥadīth, the Prophet states, "Do not commit what the Jews did, and violate Allah's prohibition using deceitful *ḥiyal*".³⁴⁵ In another report, the Prophet foretells that people from his nation will circumvent a prohibition by relying on the form, saying,

³³⁸ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p43.

³³⁹ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*. verse 7:63.

³⁴⁰ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p41-46.

³⁴¹ Ibid.

³⁴² Saheeh International, *Translation Of The Meanings Of The Glorious Quran*., verses 68:17-28.

³⁴³ Ibid. 68:17-28

³⁴⁴ Ibn Taymiyah, *Bayān al-Dalīl 'alā Ibtāl al-Taḥlīl*, p39; al-Shāṭibī, *al-Muwāfaqāt*, 3, p110.

³⁴⁵ Reported in al-'Ukbarī, *Ibtāl al-Ḥiyāl*, p112. The authenticity of this ḥadīth was regarded as *ḥasan* (good) by Ibn Taymiyah and Ibn kathīr. See: al-Maqdisī, "Takhrij Ḥadīth lā Tartakibū mā Artakabat al-Yahūd," *Multaqā Ahl al-Ḥadīth*, <http://www.ahlalhdeth.com/vb/showthread.php?t=53252>. accessed 8 March 2012.

“There will be some of my nation who will make wine [and intoxicants] legal by changing its name”.³⁴⁶ A third *ḥadīth* on this subject reads:

Narrated Jabir bin ‘Abdullah: I heard Allah’s Apostle, in the year of the Conquest of Mecca, saying, “Allah and His Apostle made illegal the trade of alcohol, dead animals, pigs and idols”. The people asked, “O Allah’s Apostle! What about the fat of dead animals, for it was used for greasing the boats and the hides; and people use it for lights?” He said, “No, it is illegal.” Allah’s Apostle further said, “May Allah curse the Jews, for Allah made the fat (of animals) illegal for them, yet they melted the fat and sold it and ate its price”.³⁴⁷

This *ḥadīth* shows that although the form and name of the fat changed after it is melted, it remains forbidden to benefit from the substance by using or selling it. Therefore, the text indicates that any legal ruse used to achieve illegitimate ends would not change the original fact of the prohibition against those ends.³⁴⁸

The Prophet also warned against some practises that might be used in avoiding the payment of *zakāh*. These are similar to tactics used by present-day accountants to avoid or reduce taxes. The *ḥadīth* reads:

Narrated Anas: Abu Bakr wrote to me what was made compulsory by Allah’s Apostle and that was [regarding the payments of *zakāh*]: Neither the property of different people may be taken together nor the joint property may be split for fear of [paying more, or receiving less] *zakāh*.³⁴⁹

Ibn al-Qayyim³⁵⁰ argues this is clear evidence for prohibiting the use of *ḥīlah*. Al-Khaṣṣāf of the Ḥanafī School accepts that such a person is committing a sin in avoiding *zakāh* by selling the property before the due date of *zakāh*. However, he

³⁴⁶ Aḥmad shu‘ayb al-Nasā’i, *al-Mujtabā min al-Sunan*, ed. ‘Abd al-Fattāḥ Abū Ghuddah, 2nd ed., vol. 8 (Maktab al-Maṭbū‘āt al-Islāmiyyah 1986), p312.

³⁴⁷ Muhammad Ismā‘īl al-Bukhārī, "Sahih al-Bukhari," Sunnah.com, <http://sunnah.com/urn/21000>. accessed 20 April 2012.

³⁴⁸ Ibn Taymiyah, *Bayān al-Dalīl ‘alā Ibtāl al-Taḥlīl*, p58; Muhammad Tahir Mansoori, "Use of Ḥiyal in Islamic Finance and its Sharī‘ah Legitimacy," *Journal of Islamic Business and Management* 1, no. 1 (2011): p77.

³⁴⁹ al-Bukhārī, "Sahih al-Bukhari". Vol. 9, Book 86, *Hadith* 87

³⁵⁰ Ibn al-Qayyim, *I‘lām al-Mawqī‘ayn ‘an Rab al-‘Ālamīn*, 3, p208.

argued that judicially, this person's action is valid, since his act appears to be merely a permissible trade.³⁵¹

The argument of invalidating *hīlah* contracts is also supported by the prophetic ḥadīth which states, "The reward of deeds depends upon the intentions and every person will get the reward according to what he has intended".³⁵² Ibn al-Qayyim³⁵³ deems this ḥadīth sufficient to invalidate *hīlah*. He argues that it shows that deeds follow motive and a person can only get what he intended. If he intended usury by a contract of sale, then he is a usurer.³⁵⁴ However, this ḥadīth does not directly support the argument of Ibn al-Qayyim. It seems directed to address the accountability aspect of *hīlah* in the hereafter, rather than the validity aspect in this world, and the former is not disputed by pro-*hīlah* schools of thought. All scholars agree that using *hīlah* in a deceptive manner is not permissible.³⁵⁵ Ibn Ḥajar al-ʿAsqalānī,³⁵⁶ a Shāfiʿī scholar, stated in his commentary on this ḥadīth that whoever intended the collection of usury through the contract of sale is not exempted from sins. Likewise, any means used to circumvent a forbidden matter is prohibited, as there is no difference between the prohibition of the illegitimate end and the prohibition of the means used to reach the forbidden end.³⁵⁷

In addition to drawing on tradition, the Mālikī and Ḥanbalī schools of thought provide many legal maxims and rational arguments to support their position.³⁵⁸ One argument is that by prohibiting usury, for example, the lawgiver intends to achieve a

³⁵¹ al-Khaṣṣāf, *Kitāb al-Ḥiyal*, p6.

³⁵² al-Bukhārī, "Sahih al-Bukhari". Vol. 1, Book 1, *Hadith* 1

³⁵³ Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p164.

³⁵⁴ Ibid.

³⁵⁵ Abozaid and Dusuki, "The Challenges of Realizing Maqasid al-Shari'ah in Islamic Banking and Finance," p15.

³⁵⁶ al-ʿAsqalānī, *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*, 12, p328.

³⁵⁷ Ibid.

³⁵⁸ See: Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p111-25; Rosman, "al-Ḥiyal wa al-Makhārij fī al-Mu'āmalāt al-Maṣrifīyyah al-Islāmiyyah," p145-49.

benefit (*jalb al-maṣlaḥah*) and prevent harm (*dar' al-mafsadah*). It is inconceivable that the lawgiver will prohibit something and then permit, let alone instruct, others to achieve it through deception. If the law were to recognise a form of sale contract intended to collect usury, or a sham transaction intended to avoid *zakāh*, then it would be enforcing what is prohibited, evading obligations, and aiding and abetting sins. This cannot be authorised under the ruling of Shari'ah.³⁵⁹

Moreover, Ibn Taymiyah and Ibn al-Qayyim³⁶⁰ argue that the harm which the lawgiver has forbidden usury to prevent exists further in the legal ruses used to circumvent the proscription of usury. This is because to achieve the desirable illegitimate ends, multiple transactions and extra efforts are required by all parties. Accordingly, Shari'ah cannot ban a harmful action and permit a more harmful one.³⁶¹

In addition, al-Muzayni³⁶² argues that some of these *ḥiyal* have been advocated by jurists on individual cases as exceptions to the general rule. However, applying them in a systemic way, as financial institutions currently do, removes their legitimacy. If classical scholars had known about the current implementation of their view, they would rule differently.³⁶³

The arguments of the pro-*ḥīlah* school seem to be directed towards protecting judicial certainty, while the anti-*ḥīlah* argument aims to protect the welfare of society

³⁵⁹ Ibn Taymiyah, *Majmū' Fatāwā Shaykh al-Islām Ibn Taymiyah*, 20, p348; Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p121; Khan, "The Mohammedan Laws against Usury and How They Are Evaded," p236.

³⁶⁰ See: Aḥmad ibn 'Abd al-Ḥalīm Ibn Taymiyah, *Majmū' Fatāwā Shaykh al-Islām Ibn Taymiyah*, ed. Abd al-Raḥmān Ibn Qāsīm, vol. 29 (Mujamma' al-Malik Fahd liṭibā'at al-Muṣḥaf al-Sharīf, 2004), p445; Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p113.

³⁶¹ See: Ibn Taymiyah, *Majmū' Fatāwā Shaykh al-Islām Ibn Taymiyah*, 29, p445; Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p113.

³⁶² 'Uthmān Zāhūr, "Bay' al-Maḥāwīj", *al-Āqtiṣādiyyah*, 2 September 2007 http://www.aleqt.com/2007/09/02/article_106741.html. accessed 26 March 2012.

³⁶³ See: Ibrāhīm, *al-Ḥiyal al-Fiqhiyyah fī al-Mu'āmalāt al-Māliyyah*, p31; Ibn Taymiyah, *al-Fatāwā al-Kubrā*, 6, p98.

by achieving the objectives of the law.³⁶⁴ Nevertheless, the pro-*hīlah* argument arises in a judicial context where a contract is disputed before a judge, and therefore it does not justify the current practise of creative Shari‘ah compliance in the Islamic finance industry. More criticisms are directed at Shari‘ah-compliant products for focusing on form over substance at the structuring and approving stages rather than the litigation stage.³⁶⁵ Unlike judges, Shari‘ah supervisory boards are assumed to oversee the permissibility aspect as well as the validity aspect.

2.6. Conclusion

This chapter has investigated whether creative Shari‘ah compliance is a phenomenon new to Islamic law and concluded that it is not: Shari‘ah scholars have addressed the practise under the term *hīlah* (a legal ruse) since the classical period of Islam. The chapter examined the position of Islamic schools of thought on *hīlah* and surveyed whether classical Islamic jurisprudence justifies using *hiyal* to practise creative Shari‘ah compliance.

The research argued for a distinction between two notions when addressing the issue: permissibility (*ṣaḥiḥ diyānatan*) and validity (*ṣaḥiḥ qaḍā’an*). From a permissibility perspective (*al-ḥukm al-taklīfī*), it concluded that there is no authority for utilising a form to circumvent the spirit of Shari‘ah law in finance. However, from a judicial validity perspective (*al-ḥukm al-waḍ’ī*), if a dispute regarding such a contract comes before a judge, it can be deemed valid according to some schools of thought, such as Ḥanafī and Shāfi‘ī.

³⁶⁴ See: al-Qurashī, *Ishkālīyyah al-Ḥiyal fī al-Baḥṭh al-Fiqhī*, p200; Coulson, *A History of Islamic Law*, p99; Powers, *Intent in Islamic Law : Motive and Meaning in Medieval Sunni Fiqh*, p119.

³⁶⁵ See for example: Wā’il Mahddī, "Ṣāliḥ Kāmil: Aghlab Muntajāt al-Bunūk al-Islāmiyyah Ghayr Islāmiyyah," *ArabianBusiness.com* <http://www.arabianbusiness.com/arabic/517729>. accessed 10 November 2010; Howladar, "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance".

In addition, the research showed that there is confusion between permissible *hīlah* and prohibited *hīlah*. While the former serves to conclude illegitimate ends, the latter achieves a result that does not contradict the spirit of the law. Scholars seem to favour referring to the latter by the term *makhraj fiqhī* (jurisprudential leeway), while using *hīlah* to refer to unlawful ruses.

Classical jurists accepted some *hīlah* on individual cases as an exception to the general rule or in the judicial context. However, applying a *hīlah* on a systemic level, as many financial institutions currently do, removes its legitimacy. Accordingly, Shari‘ah supervisory boards as institutions should not rely on such precedents to structure or Islamise financial products. Modern economic and finance knowledge put contemporary scholars in a better position than that of classical jurists to determine whether a certain product complies with the spirit of Islamic law or not. Insisting on justifying the use of some *hīlah* because they were mentioned in the classical literature would only harm the industry of Islamic finance. Ultimately, people would come to realise that there is no difference between conventional products and so-called Shari‘ah-compliant products except that the latter are more expensive!

Chapter Three:

***Tawarruq* as a Case Study of Creative Shari‘ah Compliance**

3.1. Introduction

The previous chapter discussed the issue of form and substance in Islamic finance and whether the practise of creative Shari‘ah compliance can be justified within that framework. This chapter illustrates creative Shari‘ah compliance in the Islamic finance industry by examining *tawarruq*, one of the most common structures used by institutions offering Shari‘ah-compliant products and services.

The chapter is structured in seven parts including this introduction. Part 3.2 briefly defines the concept of *tawarruq* in Islamic jurisprudence and explains why it has been selected as a case study for creative Shari‘ah compliance; Part 3.3 provides an overview of the historical development of *tawarruq*; Part 3.4 addresses the main differences between jurisprudential and organised *tawarruq*; Part 3.5 illustrates common forms of organised *tawarruq* used in credit facility and liquidity management; Part 3.6 examines Shari‘ah jurists’ views regarding jurisprudential and organised *tawarruq*; and finally, Part 3.7 concludes the chapter.

3.2. Definition of *Tawarruq* and Selection Rationale

In Islamic jurisprudence literature,³⁶⁶ *tawarruq*³⁶⁷ is defined as a form of finance wherein buyer A purchases a commodity from a seller for a deferred payment and then resells it to buyer B for cash at a price that is usually lower than the original cost. Buyer A does not intend to use the commodity, but rather purchases it intending to sell it to obtain liquidity. When buyer A first purchases the commodity, he has no

³⁶⁶ While the term *Tawarruq* has been mainly used by the Ḥanbalī School, other schools of thought have included this contract under *‘īnah* transaction. See Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyyah*, p14.

³⁶⁷ Khan, *Islamic Economics and Finance : a Glossary*, p26 & 182; El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p64-68.

arrangement to sell it to buyer B. However, as Kahf and other researchers note,³⁶⁸ this classical definition of *tawarruq* is far removed from *tawarruq* as implemented today in the financial industry, since institutions offering Islamic financial services (IIFS) play an intermediary role in this series of transactions and arrange all aspects of it. To differentiate between the two realizations of *tawarruq*, the contemporary literature often refers to the former as *al-tawarruq alfiqh* (jurisprudential *tawarruq*) and the latter as *al-tawarruq al-Munazm* or *al-Maṣrifī* (organised or banking *tawarruq*).³⁶⁹ The differences between these two concepts are discussed in more detail in part 3.4³⁷⁰

This thesis uses *tawarruq* as a case study for three main reasons. First, *tawarruq* is by and large the most commonly used product in the industry for liquidity management and credit finance.³⁷¹ It is the main financing structure for more than £600 billion in the Islamic finance industry. Mashal estimates that out of all liquidity management that uses Shari‘ah-compliant tools, more than 95% uses *tawarruq*.³⁷² In Saudi Arabia, *tawarruq* financing is the most popular financial instrument, accounting for 183 billion riyals, which represents 67% of funding in the Saudi Islamic finance market.³⁷³ Moreover, according to Issa, 75% of individuals in Saudi Arabia and Gulf Cooperation Council (GCC) countries who buy cars via banks practise *tawarruq* by reselling to a third party to obtain liquidity.³⁷⁴

³⁶⁸ Monzer Kahf, "Outlines Of a Brief Framework of Tawarruq (Cash Procurement) And Securitization In Shariah and Islamic Banking ", (2004) http://monzer.kahf.com/papers/english/a_brief_framework_of_Tawarruq_AND_SECURITIZATION.pdf accessed 10 November 2013.

³⁶⁹ Salah AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia" (paper presented at the IIUM International Conference on Islamic Banking and Finance, Kuala Lumpur 23-25/4/ 2007), p2..

³⁷⁰ See Part 3.4.

³⁷¹ Nourah Aleshaikh, "Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place" (Durham University, 2011), p50.

³⁷² ‘Abd al-Hādī Ḥabtūr "Mukhtaṣūn: al-Bunūk al-Islāmiyah tastakhdīm al-Tawarruq fī dārah al-Suūlah ruḡhm al-Taḥafuzāt al-Shar‘iyyh", *al-Āqtiṣādiyyah*, 8 January 2012 http://www.aleqt.com/2012/01/08/article_614257.html. accessed 10 November 2013.

³⁷³ Aleshaikh, "Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place," p72.

³⁷⁴ ‘Isā, " Taṭbīqāt al-Tawarruq wa Astikhdāmātuh fī al-‘amal al-Maṣrifī al-Islāmī " p463.

The second reason to choose *tawarruq* as a case study is that despite its popularity, it has attracted a lot of criticism with regard to its Shari'ah compliance.³⁷⁵ In recent years, many products offered by IIFS, such as *murābahah* and some *Ṣukūk* structures, have been under attack by many Shari'ah scholars. However, *tawarruq* as practised by IIFS has received the strongest objection from Shari'ah scholars. This was especially the case in 2009, when the International Islamic Fiqh Academy of the Organisation of the Islamic Conference (OIC),³⁷⁶ one of the most highly ranked bodies of Shari'ah scholars, issued its *fatwa* prohibiting organised *tawarruq*.

Finally, *tawarruq* provides a good example of creative Shari'ah compliance with the objectives of Islamic law. In addition to its secure return, it shares many features of conventional finance and poses a lower risk and cost in comparison to other Shari'ah-compliant products based on profit- and loss-sharing.³⁷⁷ A further benefit is its general acceptance by regulators in many jurisdictions, including non-Muslim countries like the United Kingdom.³⁷⁸

3.3. The Development of *Tawarruq*

To fully understand the jurisprudential discussion surrounding *tawarruq*, it is important to understand how it has developed from the time of classical Shari'ah jurists up to the modern practises of IIFS. The development of *tawarruq* can be categorised into three stages:

³⁷⁵ Rafe Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?* (Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2009), p1.

³⁷⁶ OIC Fiqh Academy, "Resolution 179 (19/5)," <http://www.kantakji.com/fiqh/Files/Fatawa/w246.pdf>. accessed 10 May 2013.

³⁷⁷ Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?"

³⁷⁸ See Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?*, p29.

3.3.1. *Jurisprudential Tawarruq*

Jurisprudential *tawarruq* is usually executed by individuals and takes place outside the financial system.³⁷⁹ It has been the traditional way for Muslims to obtain liquidity. In this system, a commodity, such as wheat or sugar in the past or cars today, is bought on a deferred basis and then sold on the spot for a lower price. Most *fatwa* that deem *tawarruq* permissible are directed towards this type of *tawarruq*.³⁸⁰ Other names given to this type are *al-tawarruq al-fardī*³⁸¹ (individualised *tawarruq*), classical *tawarruq*, and non-organised *tawarruq*.

3.3.2. *Partly Organised Tawarruq*

This type has been one of the most popular methods of obtaining cash in recent years.³⁸² In this case, the bank sells a commodity—usually a car or a stock share—to its client, who later sells it to a third party without the bank's interference. This structure has been approved by many Shari'ah supervisory boards (SSBs) subject to certain conditions.³⁸³

3.3.3. *Fully Organised Tawarruq*

In this type of *tawarruq*, IIFS handle and arrange all aspects of the transactions, starting with buying a commodity on the market and selling it to a client on deferred terms. The IIFS then acts as an agent, selling the commodity on behalf of the client in the market and finally depositing the cash into the client's account.³⁸⁴ This

³⁷⁹ Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyyah*, p17.

³⁸⁰ Ibid.

³⁸¹ Shochrul Rohmatul Ajija, Mia Fathia, and Agusdiwana Suarni, *Tawarruq: Issue & Challenge*, (Brunei Darussalam 2010), http://www.researchgate.net/publication/215447064_TAWARRUQ_ISSUES_AND_CHALLENGES accessed Access Date. p3; Aleshaikh, "Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place," p30.

³⁸² 'Isā, " Taṭbīqāt al-Tawarruq wa Astikhdāmātuh fī al-ʿamal al-Maṣrifī al-Islāmī " p463.

³⁸³ See, for example, Mohamed Elgari, "al-Tawarruq Kamā tujrīh al-Maṣrif " (paper presented at the 17th session of the Islamic Fiqh Academy, Makkah, 13-17/12/2003).

³⁸⁴ Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyyah*, p18.; Kahf, "Outlines Of a Brief Framework of Tawarruq (Cash Procurement) And Securitization In Shariah and Islamic Banking ".

development is not surprising, given that it reduces the time and cost associated with transactions such as delivery, storage, shipping, and marketing.³⁸⁵ Since neither IIFS nor their clients are interested in the commodity, they will welcome any arrangement that might relieve them of the extra burden of handling it.

Fully organised *tawarruq* was first offered in 2000 by the Commercial Bank (NCB)³⁸⁶ and several banks in Saudi Arabia, and other IIFS in GCC countries followed shortly.³⁸⁷ IIFS utilised the classical concept to offer a Shari‘ah-compliant product for financing and to be able to compete in the credit market, which was and is dominated by conventional institutions.³⁸⁸ Today *tawarruq* is offered in most jurisdictions where Islamic finance is practised, including Saudi Arabia and the United Kingdom.

Diagrams 1 and 2 show typical examples of jurisprudential and fully organised *tawarruq*.

³⁸⁵ Sami Al-Suwailem "Tawarruq Banking Products" (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009), p22.

³⁸⁶ AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia," p3.

³⁸⁷ Ibrahim Fadhil Dabu, "Tawarruq, Its Reality and Types" (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009).

³⁸⁸ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p5.

Diagram 1. Jurisprudential *Tawarruq*

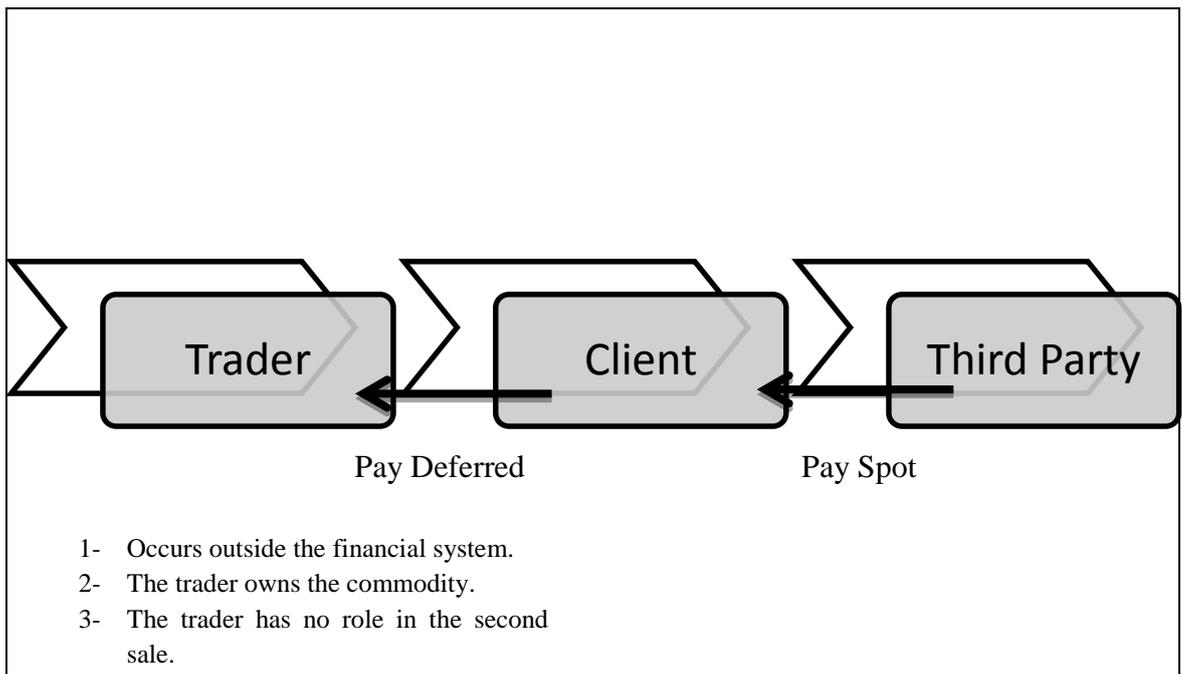
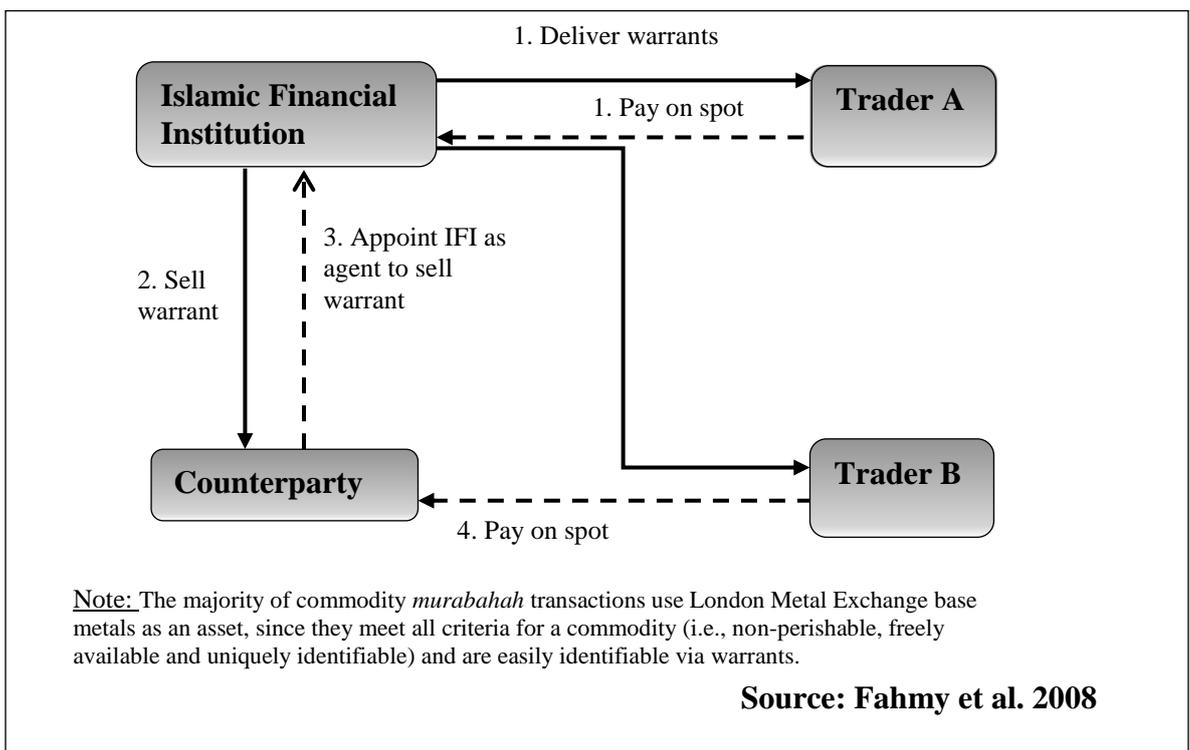


Diagram 2. Organised *Tawarruq*



3.4. The Differences between Jurisprudential and Organised *Tawarruq*

This section addresses the main differences between jurisprudential and organised *tawarruq*, providing a basis for understanding the arguments against *tawarruq*. In jurisprudential *tawarruq*, the commodity used in the transaction is usually owned by a merchant who tends to sell his stock for cash and on deferred payment. In organised *tawarruq*, the financier does not own the commodity before the clients approach him for financing, and the financier only buys the commodity to use it in the *tawarruq* transaction.³⁸⁹

Another contrast between the two kinds of *tawarruq* is the knowledge of the parties involved. In jurisprudential *tawarruq*, on the one hand, the merchant is not necessarily aware of the buyer's intention, and he is not involved in the second sale of the commodity. In organised *tawarruq*, on the other hand, neither party is actually interested in the commodity; both know it is only a means of obtaining income.³⁹⁰ IIFS assist in the whole process, which includes acting as agents to resell the commodity on behalf of the client. In fact, in large *tawarruq* transactions, the link between the three contracts is expressed in a legal document.³⁹¹ Moreover, to mitigate price volatility, IIFS usually have agreements in place with other companies to repurchase the commodities used in *tawarruq* transactions at a pre-set price.³⁹² In some cases,³⁹³ the same commodity will go back to the first seller and might be used over and over to finance other clients, a practise which casts doubt over the legitimacy of these sales contracts.

³⁸⁹Muhammad Taqi Usmani, "Verdicts on At-Tawarruq and Its Banking Applications" (paper presented at the The 17th session of the International Islamic Fiqh Academy, Makkah, 13- 17/12/ 2003), p15; Al-Suwailem "Tawarruq Banking Products," p21.

³⁹⁰ AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia," p7.

³⁹¹ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p23.

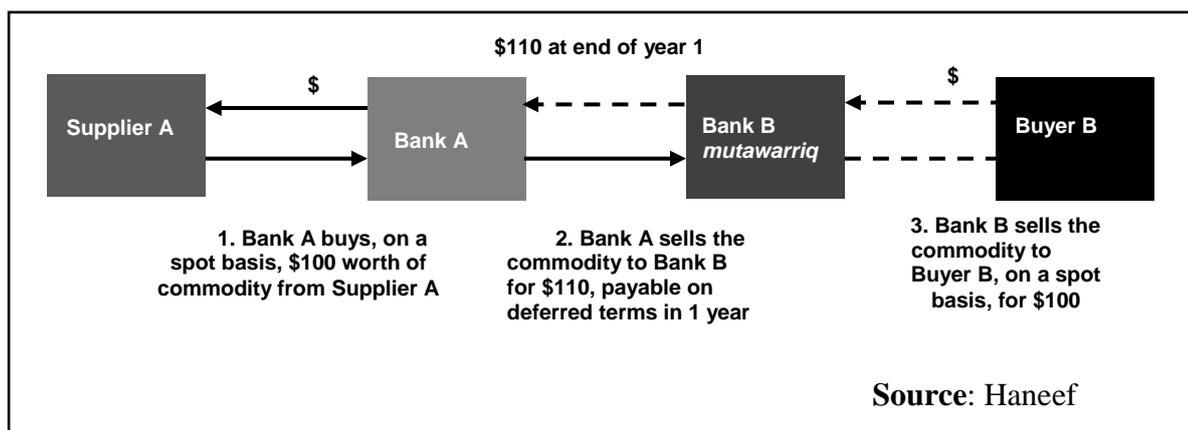
³⁹²Al-Suwailem "Tawarruq Banking Products," p22. Ajjija, Fathia, and Suarni, *Tawarruq: Issue & Challenge*. p17.

³⁹³ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p28.

3.5. Forms of *Tawarruq*

Tawarruq can take different structures in the current Islamic industry, but it is mostly used by IIFS either as a liquidity facility (e.g., inter-bank placement) or as a credit facility (e.g., consumer credit financing). The following charts illustrate some of the most common models of *tawarruq* in the industry.

Diagram 3. Inter-bank placement



Inter-bank placement (Diagram 3) is a three-step process:

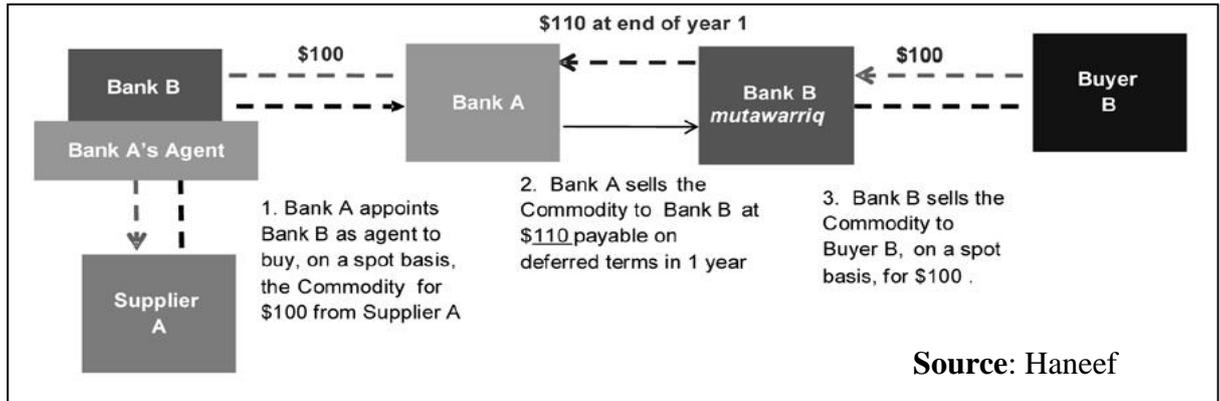
1. Bank B, which needs some liquidity, will arrange to buy commodities on deferred terms from Bank A, which has extra cash. The general terms of *tawarruq* inter-bank placements between the two banks are usually agreed before any *tawarruq* transaction takes place.
2. Bank A will purchase the commodity from Supplier A for an immediate payment, and then resell it to Bank B for a deferred payment.
3. Bank B will then sell the commodity to Buyer B on a spot-payment basis and get the liquidity it needs.³⁹⁴

However, if Bank A has no experience dealing with the commodity market, it might appoint Bank B to act as an agent for it to buy the commodity for an immediate

³⁹⁴ Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?*, p4.

payment. Bank A then sells the commodity plus a profit to Bank B, which will be paid on a deferred basis. Bank B then sells the commodity to Buyer B on a spot-payment basis and get the liquidity it needs. The process is shown in Diagram 4.

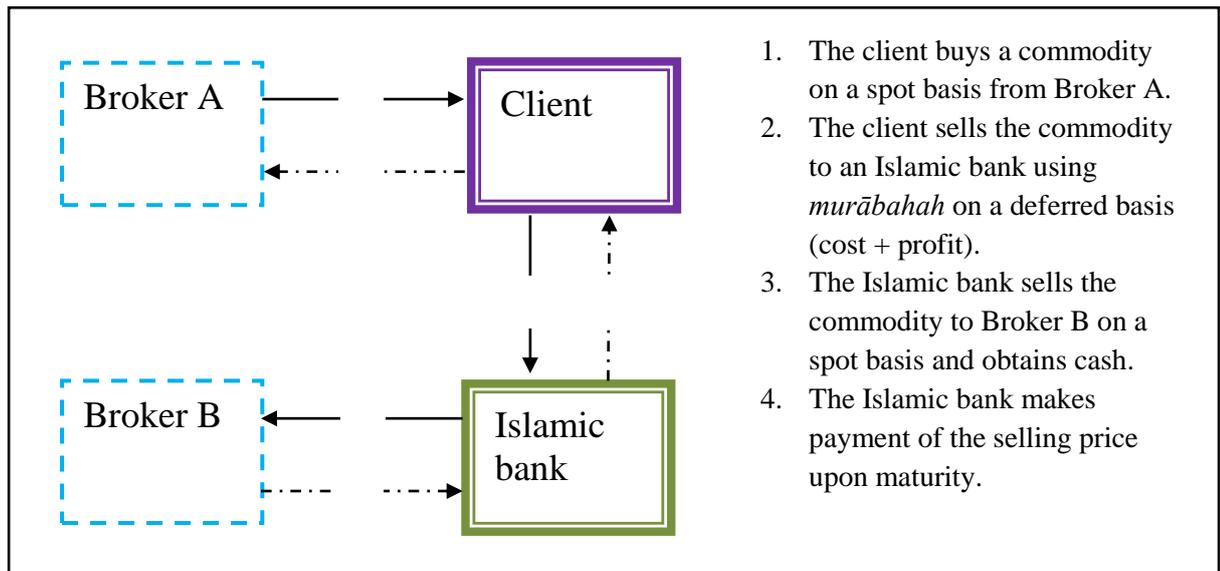
Diagram 4. Inter-bank placement



Another form practised in the industry, known as reverse *tawarruq*,³⁹⁵ is used as a deposit-mobilising instrument. In this form, the client is using *tawarruq* to receive a fixed return for his deposit. The client will buy a commodity or appoint the bank as an agent to buy it for him. He will then sell it to the bank on deferred terms. The bank then will sell it in the market on a spot basis and use the capital to finance another client. The form is illustrated in Diagram 5.

³⁹⁵ Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p4; Al-Suwailem "Tawarruq Banking Products," p38.

Diagram 5. Reverse *Tawarruq*



Modified from Dusuki

3.6. Shari‘ah Jurists’ Views on *Tawarruq*

This section summarizes the Shari‘ah jurists’ views regarding jurisprudential and organised *tawarruq*. The discussion in this section focuses on the latter, which includes partly and fully organised *tawarruq*, since those are the forms most commonly practised in the Islamic finance industry.

3.6.1. *Jurisprudential Tawarruq*

The literature³⁹⁶ shows that Shari‘ah scholars have three different views on jurisprudential *tawarruq*:

³⁹⁶ The discussion in this section is based on the following references: ‘Ali al-Sālūs "al-‘īnah wa al-Tawarruq wa al-Tawarruq al-Maṣrifī" (paper presented at the The 17th session of the International Islamic Fiqh Academ, Makkah, 13- 17 /12/2003); Elgari, "al-Tawarruq Kamā tujrih al-Maṣārif "; Al-Suwailem "Tawarruq Banking Products."; Ibrahim Fadhil Dabu, "Tawarruq, Its Reality and Types" (ibid.); Fahmy et al., "Revisiting OIC Fiqh Academy Rules on Organised Tawarruq"; Ajija, Fathia, and Suarni, *Tawarruq: Issue & Challenge*; Usmani, "Verdicts on At-Tawarruq and Its Banking Applications."; Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*; Aleshaikh, "Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place," p29; Dabu, "Tawarruq, Its Reality and Types."; Hanā’ al-Ḥuwayfī, "al-Tawarruq ḥaqīqatuh , Anwā’uuh" (ibid.).

1. The majority of scholars, including those from the Ḥanafī and Mālikī schools as well as some within the Ḥanbalī School, deem *tawarruq* as *makrūh* (discouraged).³⁹⁷
2. Another view within the Ḥanbalī School, upheld by prominent scholars Ibn Taymiyah (d.728/1328) and Ibn al-Qayyim (d.751/1350), deems *tawarruq* as *muḥarram* (prohibited).³⁹⁸
3. The Shāfi‘ī School regards *tawarruq* as *mubāḥ* (permissible); this is also the dominant opinion within the Ḥanbalī School as well as the stance of Abu Yosef, a prominent jurist within the Ḥanafī School. Although this view is favoured by the majority of contemporary Shari‘ah scholars and *fatwa* bodies,³⁹⁹ many prominent contemporary Shari‘ah scholars⁴⁰⁰ deem jurisprudential *tawarruq* as *muḥarram* (prohibited).

3.6.2. Arguments against Organised Tawarruq

Contemporary Shari‘ah scholars have two different views regarding the permissibility of organised *tawarruq*. The majority of contemporary scholars deem organised *tawarruq* impermissible.⁴⁰¹ This is also the view of the International Islamic Fiqh Academy of the OIC.⁴⁰² These scholars base their view on several Shari‘ah, economic, and *maslahah* (public interest) arguments.

³⁹⁷ Zayn Ibn Ibrāhīm Bakr, *al-Baḥar al-Rā‘iq* vol. 6 (Beirut Dār al-Ma‘rifah), p256; ‘Alī al-Mirdāwī, *al-Inṣāf fī ma‘rifah al-Rājiḥ min al-Khilāf* vol. 11 (1956), p195; Muḥammad al-Ḥaṭṭāb *Mawāhib al-Jalīl sharḥ Mukhtaṣar Khalīl* vol. 4 (Beirut: Dār al-Fikr), p405; ‘AbdAllāh al-Sa‘īdī "al-Tawarruq kamā tujrīh al-Maṣārif fī al-Waqt al-ḥādir " *Majalah al-Mjama‘ al-Fiqh al-Islāmi*, no. 18 (2004): p197.

³⁹⁸ Muḥammad bn Abī Bakr Ibn al-Qayyim, *Tahdhīb Sunan Abī Dāwd*, vol. 5 (Makkah: Dar al-baz, 1980), p801. al-Mirdāwī, *al-Inṣāf fī ma‘rifah al-Rājiḥ min al-Khilāf* 11, p195.

³⁹⁹ Like the Islamic Fiqh Council of the Muslim World League, the Permanent Committee for Islamic Research and Issuing Fatwas in Saudi, and many SSBs in IIFS. See al-Ḥuwayfī, "al-Tawarruq ḥaqīqatuh , Anwā‘uuh," p13.

⁴⁰⁰ Like Hssan Hammad Hssan , Rifeq Al-Massry, Saleh Al hossian. See Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyyah*, p29.

⁴⁰¹ Ibid., p32.

⁴⁰² OIC Fiqh Academy, "Resolution 179 (19/5)". It is worth noting that AAOIFI’s Standard 30 on Tawarruq does not conflict with the OIC decision. For a detailed discussion, see Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?".

First, from an Islamic jurisprudence perspective, opponents of organised *tawarruq* argue that it is *hīlah* (a legal ruse) to circumvent the prohibition of *ribā* (usury), since the ultimate goal of structuring three contracts in this order is to provide a sum to be paid later with a fixed return. This principle is illustrated in the following example.⁴⁰³ Two people need financing of £10,000. The first one applied for a £10,000 usurious loan to be paid back within two years. The second person applied for an organised *tawarruq*. The bank bought an amount of iron for £10,000, sold it to the second person for £11,000 on a deferred term of two years, and then sold it to the market on behalf of the client for £10,000. The final outcome is that both people are charged a sum greater than what they have received, and the bank is the creditor in both situations. In fact, organised *tawarruq* might be more costly, since the price of the commodity may change, and the bank may charge administration and brokerage fees. IIFS and their clients are not interested in these commodities, which have only been used as a means to overcome the restrictions on giving a usurious loan in Shari‘ah.⁴⁰⁴ It is not unusual to find that some clients are not aware of the commodity which they—in theory—bought and sold during the process of organised *tawarruq*.⁴⁰⁵ For instance, IIFS often use palladium, a commodity unfamiliar to many individual consumers, in their *tawarruq* financing.

Second, opponents of organised *tawarruq* have objected that the use of commodities in these transactions does not comply with Islamic legal standards. They argue that these transactions breach one of the fundamental tenets of Shari‘ah law,

⁴⁰³ AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia," p10.

⁴⁰⁴ Al-Suwailem "Tawarruq Banking Products," p35; Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?"

⁴⁰⁵ Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyyah*, p37.

which states that goods must be valuable and useable for legitimate purposes.⁴⁰⁶ A commodity must also be specified, and it should match the description provided to the buyer. The scholarly concern surrounds the genuineness of some of the goods used in organised *tawarruq*. For instance, Dr Al-Qara Daghi,⁴⁰⁷ a renowned Shari'ah scholar in the industry, describes an organised *tawarruq* contract that was submitted to the Shari'ah board for approval in which the underlying commodity sold was junk Russian aluminium. The broker chose this item deliberately for *tawarruq* because it was not possible to sell it on the market. Another issue is that there are no assertions that the same goods will not be sold to more than one buyer at the same time. Dusuki⁴⁰⁸ considers the problem of fictitious commodities a key reason for Shari'ah scholars to prohibit organised *tawarruq*.

In addition, Shari'ah scholars have raised concerns related to the possession and the delivery of goods used in organised *tawarruq*. For a contract to be valid under Shari'ah, the seller must own the commodity before selling it. This is because a sale contract is intended for transferring the ownership of the item to the buyer and the ownership of the payment to the seller. Accordingly, selling a commodity before acquiring possession of it or restricting the buyer from controlling what he bought defies the purpose of the sale contract and invalidates the transaction. In some organised *tawarruq* deals, the possession of the commodity does not occur. This is especially the case when the contract includes a clause stating that the buyer should

⁴⁰⁶ Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p15.

⁴⁰⁷ Ali Al-Qara Daghi " Murāj'at Fatāwā Nadwat al-Barakah. ," <http://www.isra.my/media-centre/downloads.html?task=finish&cid=102&catid=21>. accessed 10 Novmber 2013).

⁴⁰⁸ Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p15.

not intend to take delivery or imposing extra fees if he wants to do so.⁴⁰⁹ Dusuki⁴¹⁰ notes that such delivery restrictions have become a standard practise in the market.

Furthermore, to mitigate the risk of price volatility mentioned earlier, some IIFS contract with a third party to repurchase the commodities used in the *tawarruq* at a fixed price regardless of their actual price that day in the market.⁴¹¹ In this situation, IIFS commit to selling something before owning it and before being appointed as agents by the principals (i.e., the clients).⁴¹² Moreover, this arrangement breaches the agency agreement, because if the price goes up in the market, IIFS will be acting against the best interests of their principal since they have a standing agreement with a third party to buy this commodity at a fixed price. This indicates that the process of organised *tawarruq* aims merely to provide a sum to be paid later with a fixed return, which is labelled a profit rather than interest.

With the regard to economy, opponents offer three main objections. First, they argue that the wide use of organised *tawarruq* increases debt proliferation, creating a harmful economic impact opposed by Shari‘ah.⁴¹³ As argued by Siddiqi⁴¹⁴ earlier in this thesis,⁴¹⁵ finance based on debt is unfair because it redistributes wealth in favour of the providers of finance regardless of the productivity of the fund provided. It is also an inefficient way to create wealth, since the fund goes to the most credit-worthy debtor and not to the most productive project.

⁴⁰⁹Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?".

⁴¹⁰ Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p15; Khan, "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?".

⁴¹¹ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p41.

⁴¹² Ajija, Fathia, and Suarni, *Tawarruq: Issue & Challenge*. p16; Al-Suwailem "Tawarruq Banking Products," p31.

⁴¹³ Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p12. Fahmy et al., "Revisiting OIC Fiqh Academy Rules on Organised Tawarruq". p8.

⁴¹⁴ Siddiq, "Economics Of Tawarruq: How Its Mafasid Overwhelm The Masalih" p1-2.

⁴¹⁵ See chapter 1 at p 32.

Second, opponents criticise organised *tawarruq* for driving national capital outside the country.⁴¹⁶ The issue is that most of the commodities it uses are traded on the international market,⁴¹⁷ which results in depriving local markets and communities of national capital.

Third, organised *tawarruq* opponents also condemn the excessive profit margin IIFS make with *tawarruq* compared to the return on a conventional loan.⁴¹⁸ This is because while the interest rate is set by central banks, the profit rate is not necessarily subject to the same control, since *tawarruq* is technically a sale contract.⁴¹⁹ The flat-profit rate of *tawarruq* usually ranges from 6% to 14%. The profit “is calculated on a non-reducing balance”,⁴²⁰ resulting in consumers effectively paying a profit based on an annual percentage rate (APR) of 12% to 28%. Some IIFS tend to stress the lower flat rate rather than informing consumers about the high APR they will pay if they select *tawarruq* as a credit facility.⁴²¹ Consumers’ lack of financial knowledge might prevent them from noticing the difference.

From a public interest perspective, opponents of organised *tawarruq* present three arguments. First, they argue that approving organised *tawarruq* and similar structures raises questions about the credibility of the Islamic finance industry⁴²² in both Muslim and non-Muslim countries, because using such a structure eliminates differences between conventional finance and Islamic finance. Islamic finance has been defended by its advocates as an ethical system based on profit- and loss-sharing, and if that changed—for example, with the approval of *tawarruq*—people would soon start

⁴¹⁶ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p60.

⁴¹⁷ Elgari, "al-Tawarruq Kamā tujrīh al-Maṣārif " p15.

⁴¹⁸ Albahooth, *al-Tawarruq al-Maṣrifī al-Munaẓm wa āthāruh al-āqtiṣādiyah*, p54.

⁴¹⁹ Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?*, p24.

⁴²⁰ Ibid.

⁴²¹ Rafiq Ūnis al-Maṣrī, " al-Tawarruq fy al-Bunūk hl hū Mubārah Am Mash'ūm " Markaz Abḥāth al-Āqtiṣād al-Islāmī http://islamiccenter.kau.edu.sa/arabic/Hewar_Arbeaa/abs/164.htm. accessed 10 December 2013

⁴²² Ajija, Fathia, and Suarni, *Tawarruq: Issue & Challenge*. p17.

wondering what the difference is between a usurious loan and a Shari‘ah-compliant product.⁴²³ This might be especially the case in some countries where Shari‘ah-compliant products have tax disadvantages compared to conventional loans or mortgages.

Second, they also argue that the increasing use of organised *tawarruq* affects the need for innovation and development in the Islamic financial sector.⁴²⁴ Currently, many IIFS and research centers support and invest in the development of Shari‘ah-compliant financial products based on profit- and loss-sharing. But if the *tawarruq* were deemed to be Shari‘ah compliant, there would be no need to invest in developing further products in line with the objectives of Islamic law.

The third argument from the public interest perspective is that using such a structure hinders negotiations between IIFS and regulators.⁴²⁵ The Islamic finance industry has always argued that a conventional legal framework does not suit its needs and that IIFS need to be relieved from certain restrictions (e.g., they should be allowed to share ownership of real estate). Some central banks have started to realize that IIFS need a different framework, and progress has been made in this regard (e.g., different calculation methods of capital adequacy; special arrangements with regard to the lender of last resort). However, with IIFS increasing the use of organised *tawarruq* and similar debt-oriented products, there will be no need for these changes, since the difference between conventional financial institution and IIFS is in the process rather than the substance of the product.⁴²⁶

⁴²³ In 2011, a popular Saudi Arabian television comedy called *Tāsh Mā Tāsh (No Big Deal)* provoked a huge controversy after accusing Islamic banks of being no different from conventional banks. The episode was titled *zayd akhū ‘ubayd*, an Arabic idiom that means “cut from the same cloth. See Alarabiya, “ḥalaqah zayd akhū ‘ubayd fī ṭāsh 18 takshif wasā’il al-bunūk al-islāmiyah fī al-taḥāul biālribā”.

⁴²⁴ Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyah*, p55.

⁴²⁵ Ibid., p58.

⁴²⁶ Muḥy al-Dīn Aḥmad Aḥmad " al-Taṭbīqāt al-Maṣrifīyyah li‘aqd al-Tawarruq" (paper presented at the Dawr al-Mu’sasāt al-Maṣrifīyah fī al-āstithmār wa al-Tanmiyyah, Sharjah, UEA, 7-9 May 2002), p458.

3.6.3. Arguments Supporting Organised *Tawarruq*

Despite these arguments against organised *tawarruq*, some contemporary scholars do consider it permissible, since the general rule of sales in Islam, stated in verse 2:275 of the Quran, reads, “Allah has permitted trade and has forbidden interest”.⁴²⁷ They hold that organised *tawarruq* is nothing but a combination of sales contracts, which each meet all the conditions of a permissible contract in Islam.⁴²⁸ According to this line of thinking, the intention of combining these contracts is irrelevant and does not affect the validity of the contract. However, the permissibility of an individual contract in Shari‘ah does not mean that the whole combination of transactions is permissible. For example, the majority of Shari‘ah jurists, including those who allow organised *tawarruq*, deem *īnah* contracts (double sales) as prohibited, although they are a combination of two sale contracts.⁴²⁹

Haneef⁴³⁰ takes a more pragmatic approach than many supporters of organised *tawarruq*. Although he seems to acknowledge a similarity between organised *tawarruq* and *ribā* (usury),⁴³¹ he does not think this is the right time to renounce organised *tawarruq*. Haneef believes that the OIC ban on organised *tawarruq* reflects Shari‘ah scholars’ dissatisfaction over the direction of the devolvement of the Islamic finance industry. *Tawarruq* opponents want to send a message to IIFS that they have to change the way they offer Shari‘ah-compliant products if they wish to comply with the objectives of Shari‘ah. Haneef explains that the lack of a physical link with commodities in organised *tawarruq* transactions have made them an easy target for critics. The commodity is used only as a means of getting income, so consumers do

⁴²⁷ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

⁴²⁸ See Dusuki, *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?*, p6; al-Ḥuwaytī, "al-Tawarruq ḥaqīqatuh , Anwā' uuh," p27.

⁴²⁹ AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia," p3.

⁴³⁰ Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?*, p11.

⁴³¹ Ibid.

not care if IIFS use copper, stock shares, or even airtime to structure their credit financing.

Haneef supports his argument with a statement from a leading scholar in the Islamic finance industry and a member of many SSBs, Sheikh Taqi Usmani,⁴³² who notes that transactions such as *tawarruq* and *murabah* were tolerated by Shari‘ah scholars forty years ago, at the dawn of the Islamic finance industry, who took into consideration the circumstances of these newly established IIFS and the unfriendly nature of the conventional financial system. The move was intended to facilitate Islamic finance and to give IIFS some ground in the market. However, Usmani points out that

it was not in the calculation of the jurists who ruled to permit these procedures that these institutions would sit contentedly satisfied with these way outs for an unlimited time, adopting it as the targeted goal for the establishment of Islamic banks and the basic activity, which centres around their dealings forever.⁴³³

Usmani argues that today, IIFS—with their market share—can offer Shari‘ah-compliant products which in actuality do comply with the forms and the objectives of Islamic law.⁴³⁴

Haneef,⁴³⁵ however, disagrees with Usmani and other *tawarruq* opponents. According to him, the Islamic finance industry is not yet mature enough to influence the financial system. Specifically, Haneef argues, the Islamic finance industry does not have enough market share to make a shift in the financial industry. Its global size is not large enough to adopt the ideal form of commercial financing in Shari‘ah, which is based on profit- and loss-sharing. To support his point, he⁴³⁶ cites the industry in Malaysia, where the government has been promoting Islamic finance since

⁴³² Usmani, "Verdicts on At-Tawarruq and Its Banking Applications," p18.

⁴³³ Ibid.

⁴³⁴ Ibid.

⁴³⁵ Haneef, *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?*, p15.

⁴³⁶ Ibid., p16.

1980. However, in 2009, the share of Islamic banking made up only 13% of the total banking market. With this small market share, IIFS have no power to drive consumers towards profit- and loss-sharing products or to pressure regulatory authorities to modify the financial framework to accommodate authentic Shari‘ah-compliant products.

Haneef asserts that IIFS are bound to stimulate the risk profile of conventional finance products.⁴³⁷ It is unrealistic for Shari‘ah scholars to think that IIFS, with their current market share, will be able to fundamentally shift consumers’ and regulators’ attitudes towards Islamic finance, let alone change the economic system from a debt-based system to a profit- and loss-sharing-based economy. Haneef contends that the pricing, along with the Shari‘ah compliance, is primarily what attracts consumers to Islamic finance. Islamic finance would lose its appeal if its price were higher than that of its conventional counterparts, which would be the case with the profit- and loss-sharing Shari‘ah products. Haneef believes that in order for the Islamic finance industry to survive, it must increase its share of the market even if its products are not in compliance with the ideal profit- and loss-sharing system of financing in Shari‘ah. Once IIFS control at least two thirds of the market share, they can move towards offering truly Shari‘ah-compliant products.⁴³⁸ Without gradually acquiring a huge market share, it would be impossible to shift to this ideal system.⁴³⁹

Furthermore, Haneef⁴⁴⁰ argues that if *tawarruq* has been used sensibly, it can benefit the community and fulfil its social needs. Without *tawarruq*, Muslim consumers will be forced to use conventional financing facilities. In addition, the harmful effects of *tawarruq* which Siddiqi described can also result from other

⁴³⁷ Ibid., p17.

⁴³⁸ Ibid., p20.

⁴³⁹ Ibid., p21.

⁴⁴⁰ Ibid., p22.

products, such as *murābahah* and *ijārah*, which are approved by some of the Shari‘ah scholars who oppose *tawarruq*. He also⁴⁴¹ suggests that the misuse of organised *tawarruq* should not be solved by banning it, but rather by means such as responsible marketing tactics, thoughtful credit approval, consumer suitability tests, and alternative saving plans. For instance, some IIFS take advantage of religious seasons such as Ramadan to launch their *tawarruq* marketing, encouraging consumers to accrue unnecessary debt and spend on luxury goods. Shari‘ah encourages Muslims to live within their financial ability and only use debt as a last measure for serious needs.⁴⁴² Adopting the culture of “buy now and pay later” in IIFS marketing campaigns is not in line with the teaching of Shari‘ah, and Haneef urges that SSBs prevent such disjunctions by playing a role in guiding marketing policies of the Shari‘ah-compliant products they approve.⁴⁴³

In short, Haneef⁴⁴⁴ concludes that despite the ban on organised *tawarruq*, it is unlikely that the Islamic finance industry will soon find alternatives. *Tawarruq* growth was primarily due to the fact that other alternatives were not feasible. The law in some countries, including those with Muslim majorities, was not developed to allow systems other than *tawarruq*. For example, in Saudi Arabia, regulators only chose the *tawarruq* structure out of many Shari‘ah-compliant proposals in order to finance a company-won telecom licence. Therefore, according to Haneef, *tawarruq* will remain in use among IIFS.⁴⁴⁵ He recommends that critics direct their energies towards teaching IIFS about ethical marketing and consumers’ credit-suitability tests, and that academic Shari‘ah scholars and practitioners try to find practical solutions that will enable IIFS to gradually offer products based on equity-based models. Until

⁴⁴¹ Ibid., p23.

⁴⁴² Ibid., p24.

⁴⁴³ Ibid., p25-26.

⁴⁴⁴ Ibid., p29-30.

⁴⁴⁵ Ibid., p28.

then, Haneef argues, IIFS should be allowed to offer *tawarruq* and to compete for a larger market share.

However, as this part of the chapter attests, Haneef's argument is based in pragmatism rather than in Shari'ah law. He seems to base his argument on two premises: that Islamic finance can only be applied within the banking domain, and that organised *tawarruq* is better than usury. Finding or assessing any alternative structures to organised *tawarruq* is beyond the scope of this chapter, which aims to provide a case study of creative Shari'ah compliance, or indeed of this thesis. Nevertheless, I shall briefly discuss the second premise, since it is shared by some of the opponents of organised *tawarruq*.

3.6.4. Is Tawarruq Better than Ribā?

Despite the strong criticisms of organised *tawarruq*, some of its opponents, such as AlShalhoob,⁴⁴⁶ think it is a better option than *ribā* (a usurious loan). Needless to say, this position is also shared by *tawarruq* supporters who acknowledge that it is not in line with the objectives of Shari'ah. The rationale behind this view is that although Shari'ah scholars unanimously prohibit usury, a minority of scholars believe that organised *tawarruq* is permissible. Accordingly, it is preferable to a transaction that is completely prohibited. This view allows organised *tawarruq* if a conventional loan is the only alternative.

However, not all the opponents of *tawarruq* agree with this justification. They argue it poses a higher financial and social cost than an interest-based loan,⁴⁴⁷ because of the complex nature of the structure and the series of transactions required to get the client the sum he needs. The only way to reduce the cost of these transactions is to not

⁴⁴⁶ AlShalhoob, "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia," p59.

⁴⁴⁷ Kahf, "Outlines Of a Brief Framework of Tawarruq (Cash Procurement) And Securitization In Shariah and Islamic Banking ". p3; Albahooth, *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyyah*, p59.

implement it in practise, which results in a conventional loan with more paperwork. Moreover, opponents argue that provisional solutions in the financial industry will only make the situation worse, having a negative impact on the future of the industry as well as on the economy as whole. Such provisional solutions will cast doubt on the authenticity of Islamic finance and will lead to IIFS losing their identity as institutions offering truly Shari‘ah-compliant products. This reputational damage is very difficult to repair.

What is more, opponents of *tawarruq* argue that seeking liquidity through a clearly usurious loan is better than seeking it via organised *tawarruq*. This is because when a Muslim practises usury, he knows that it is strictly prohibited and therefore will limit his dealing to situations of absolute necessity.⁴⁴⁸ On the other hand, disguising a structure that achieves the same outcome under a different name and marketing it as Shari‘ah compliant could lead consumers using this product to buy accessories and luxury goods that create unnecessary debt. In short, a Muslim might be hesitant to buy a smartphone or new laptop using a usurious loan, but he or she might be more willing to buy it using organised *tawarruq*, especially if it is marketed with comforting names like *al-tawarruq al-mubark* (the blessed *tawarruq*).⁴⁴⁹ In short, organised *tawarruq* does not carry any social, economic, or equity benefits and shares the same disadvantages as the usurious loan.⁴⁵⁰

Interestingly, the renowned classical scholar Ibn Taymiyah (d.728/1328) realised this point, which led him to advocate for the prohibition of *tawarruq* in all its forms. His student and close associate Ibn al-Qayyim (d.751/1350), also a prominent Ḥanbalī scholar, states the following regarding Ibn Taymiyah’s position on *tawarruq*:

⁴⁴⁸ *al-Tawarruq al-Maṣrif al-Munazm wa āthāruh al-āqtiṣādiyah*, p59.

⁴⁴⁹For example, see: Arab National Bank (ANB), "al-Tawarruq al-Mubark," ANB, http://www.anb.com.sa/arabic/loan_tawaruq_local.asp. accessed 10 December 2013).

⁴⁵⁰ Kahf, "Outlines of a Brief Framework of Tawarruq (Cash Procurement) and Securitization in Shari‘ah and Islamic Banking".

Our teacher (God bless his soul) forbade *tawarruq*. He was challenged on that opinion repeatedly in my presence, but never approved it. He said: "The precise economic substance for which *ribā* was forbidden is present in this contract, and transaction costs are increased through purchase and sale at a loss of some commodity. Sharia would not forbid a smaller harm and permit a greater one!"⁴⁵¹

Given the harmful consequences of *tawarruq* enumerated above, one might wonder why it has been allowed by some scholars since the early days of the Islamic state (circa 700 CE). Siddiqi⁴⁵² believes the answer is twofold. First, early jurists lived in a different economic world where debt had no major role in the economy; debt instruments barely existed, let alone a debt market. The speculation of dealers was directed at the prices of actual goods and services rather than at the prices of debt instruments. The role of debt in financing business was limited. Business and agriculture were mostly funded by personal wealth, trade credit, and partnership. Second, Siddiqi argues that earlier Shari'ah scholars lacked the tools of macroeconomic analysis; they were not able to appreciate the negative impact of *tawarruq* on the economy as a whole, while it was much easier to see the benefit of *tawarruq* for a particular situation in which liquidity was provided at the time of need. Even today, Siddiqi thinks that Shari'ah scholars' discussion has been more centred on the contractual elements of *tawarruq* rather than on the negative consequences of the *tawarruq* transaction for the economy and public policy.

3.7. Conclusion

This chapter has aimed to illustrate creative Shari'ah compliance in the Islamic finance industry by examining *tawarruq*, one of the most common structures used by IIFS. After defining *tawarruq* and its various forms, the chapter addressed Shari'ah

⁴⁵¹ Ibn al-Qayyim, *I'lām al-Mawqī'ayn 'an Rab al-'Ālamīn*, 3, p170. Translation of Dr El-Gamal (with amendments) in El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p71.

⁴⁵² Siddiq, "Economics Of Tawarruq: How Its Mafasid Overwhelm The Masalih" p6. See also, Zubair Hasan, "Islamic Finance: The Structure-Objective Mismatch and its Consequences," *ISRA International Journal of Islamic Finance* 2, no. 1 (2010): p45.

scholars' views on the permissibility of *tawarruq*. It has shown that while most scholars deem jurisprudential *tawarruq* as *makrūh* (discouraged), the majority of scholars deem organised *tawarruq* used by IIFS as prohibited and see it as *hīlah* (a legal ruse) to circumvent the Shari'ah prohibition on *ribā* (usury). The ultimate goal of the organised *tawarruq* structure is to provide a sum to be paid later with a fixed return. IIFS and their clients are not interested in the underlying commodity, which is only used as a means to overcome the restriction against giving a usurious loan in Shari'ah. Last, the chapter has argued that organised *tawarruq* is worse than *ribā* since it casts doubt on the authenticity of Shari'ah-compliant products; does not create any social, economic benefits; and has the same disadvantages as a usurious loan.

Chapter Four:

Standardisation of *Fatwas* to Reduce Creative Shari‘ah Compliance

4.1. Introduction

In the previous chapters, the thesis critically appraised justifications of creative Shari‘ah compliance practises, and chapter three provided a case study of one of the most common practises of creative Shari‘ah compliance, known as *tawarruq*. This chapter examines the inconsistency in the *fatwas* issued by Shari‘ah supervisory boards (SSBs) that reside in various financial institutions as a key factor contributing to the issue of creative Shari‘ah compliance. A product that is deemed Shari‘ah-compliant by an SSB in one institution offering Islamic financial services (IIFS) may not be regarded as such by another SSB. This inconsistency is affecting the compliance level in the industry significantly, since stakeholders are left confused about which products are Shari‘ah compliant and which are not, and about what Shari‘ah compliance means.

This chapter aims to examine the appositeness of standardisation as a mechanism to reduce conflict in the opinions of Shari‘ah scholars concerning the permissibility of financial products.⁴⁵³ The chapter is structured in six parts including this introduction. Part 4.2 defines standardisation and other relevant terms; Part 4.3 addresses the arguments for and against standardisation; Part 4.4 examines the causes of juristic differences; Part 4.5 traces the legal theories offered in classical Islamic jurisprudence to deal with this issue, suggests potential remedies, and highlights the limitations of implementing them in Islamic and secular countries; finally, Part 4.6 concludes the chapter.

⁴⁵³ The chapter is not concerned with standardising inconsistent applications of one *fatwa*, since that is more of a governance issue than a juristic one. See: Ahmad Alkhamees, "The Impact of Shari‘ah Governance Practices on Shari‘ah Compliance in Contemporary Islamic Finance," *Journal of Banking Regulation* 14, no. 2 (2012).

4.2. Standardisation: A Definition

“Standardisation” as a process or term can have different meanings depending on its usage; these meanings depend especially on disciplinary context and on the nature of the participants involved. But according to the *Oxford Dictionary of English*,⁴⁵⁴ to standardise something is to cause it “to conform to a standard” which is “used as a measure, norm, or model in comparative evaluations”. Foster⁴⁵⁵ notes that the term “standardisation” is used by financiers more than lawyers, who tend to discuss it as part of the concept of legal certainty. In the context of Islamic finance, however, standardisation can be defined as setting up global Shari‘ah standards by codifying the principles and precepts of Islamic commercial law.⁴⁵⁶

This thesis addresses two notions of standardisation: national standardisation and international standardisation. The former refers to standardisation of a specific interpretation of Shari‘ah on an Islamic financial matter which will be enforced in a national jurisdiction of one country, whereas the latter is concerned with standardisation of Shari‘ah-compliant criteria among different jurisdictions. It is worth noting that some aspects of Shari‘ah such as *‘aqīdah* (dogma) and *‘ibādāt* (rituals) are not subject to standardisation because they are deemed to be beyond the scope of *ijtihād*⁴⁵⁷ and national legislation.⁴⁵⁸ Thus, this chapter’s discussion of standardisation is limited to the domain of Islamic commercial law.

⁴⁵⁴ Angus Stevenson, "Oxford Dictionary of English," Oxford University Press, http://www.oxfordreference.com/views/BOOK_SEARCH.html?book=t140. accessed 1 November 2011.

⁴⁵⁵ Foster, "Islamic Finance Law as an Emergent Legal System," p188.

⁴⁵⁶ Wafica Ali Ghoul, "The Standardization Debate in Islamic Finance: A Case Study " (paper presented at the 8th International Conference on Islamic Economics and Finance, Doha, 18/12/2011), p2.

⁴⁵⁷ *Ijtihād* can be defined as “the processes of reasoning that the jurist employed in order to arrive at the best guess of what he thought might be the law pertaining to a particular case.” Wael B. Hallaq, *An introduction to Islamic law* (Cambridge, UK; New York: Cambridge University Press, 2009), p27.

⁴⁵⁸ Mohammad Hashim Kamali, "Shari‘ah and Civil Law: Towards a Methodology of Harmonization," *Islamic Law and Society* 14, no. 3 (2007): p397.

4.3. Why Is Standardisation Needed?

Industry leaders are increasingly becoming uneasy that inconsistencies in SSB rulings can occur in the same bank over time, between different SSBs in one country, or at the international level between SSBs operating in different jurisdictions.⁴⁵⁹ Many of these leaders have voiced their concern that the lack of consistency among SSBs *fatwas* is currently hindering the growth of Islamic finance and that unless a standard framework is adopted, the market will continue to be fragmented.⁴⁶⁰ For instance, the International Organization of Securities Commissions (IOSCO) stated in its September 2008 report that “as the Islamic securities markets continue to expand both geographically and in terms of market size, the development of regulatory standards, standardisation of documentation, practises and the ratings of products will be essential”.⁴⁶¹

4.3.1. Arguments for Standardisation

Proponents of the standardisation of Shari‘ah interpretations in the Islamic finance industry have offered several justifications. These include protecting financial stability, promoting growth, and maintaining public confidence in the Islamic finance industry; saving cost and time; increasing IIFS efficiency and international marketability; encouraging innovation and development; mitigating Shari‘ah risk; and easing the task of regulators.

One argument for supporting standardisation is that it would help to ensure financial stability, promote growth, and maintain consumer confidence in the

⁴⁵⁹ Wafik Grais and Matteo Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services," *World Bank Policy Research Working Paper 4054*(2006) <http://ssrn.com/abstract=940711> accessed 2 December 2010.

⁴⁶⁰ El Baltaji and Anwar, "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance".

⁴⁶¹ Executive Committee of The International Organization Of Securities Commissions, "Analysis of The Application of IOSCO’s Objectives And Principles of Securities Regulation For Islamic Securities Products " International Organization of Securities Commissions (IOSCO) <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD280.pdf>. accessed 17 June 2012.

market.⁴⁶² When SSBs issue conflicting *fatwas* as to whether or not a specific product is Shari‘ah compliant, they confuse not only the public, but also the practitioners in the industry.⁴⁶³ The value of the international *ṣukūk* market shrank from about \$50 billion in 2007 to about \$15 billion in 2008.⁴⁶⁴ The loss was said to be partly caused by the statement of Taqi Usmani (a leading Shari‘ah scholar within Islamic finance industry) that “many structures presenting themselves as Islamic did not meet the definition of true Shari‘ah compliance”.⁴⁶⁵

The inconsistency of Shari‘ah models results in these models’ limited mobility on the national as well as on the global levels.⁴⁶⁶ This inconsistency thus impedes the market from fulfilling its potential. An example of inconsistency on the national level is the dispute over organised *tawarruq*, as discussed in chapter three. While it is accepted by many SSBs in Saudi Arabia, it is rejected by other prominent Shari‘ah scholars in the Kingdom.⁴⁶⁷ On an international level, the contract of *‘īnah* is approved by some SSBs in Malaysia as Shari‘ah compliant, while some SSBs in Gulf Cooperation Council (GCC) countries deem it an illegitimate legal ruse employed to circumvent Shari‘ah’s prohibition of usury.⁴⁶⁸

⁴⁶² Ghoul, "The Standardization Debate in Islamic Finance: A Case Study " p4; Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". p8.

⁴⁶³ Hakimah Yaacob, Marjan Muhammad, and Edib Smolo, "International Convention For Islamic Finance: Towards Standardisation ", *ISRA Research Paper (No. 29/2011)*(2011) <http://www.isra.my/publications/research-paper/research-paper/item/858-research-paper-no-29/2011.html> accessed 20 June 2012

⁴⁶⁴ Editorial, "Shariah Auditing for the Islamic Finance Industry", *Islamic Finance News* 9th November 2011 http://www.audit.gov.my/intranet/images/pdf/AAN/2011/koleksi_perpustakaan/vol.%208%20issue%2044%209%20november%202011%20-%20shariah%20auditing%20for%20the%20islamic%20finance%20industry.pdf. accessed 17 June 2012.

⁴⁶⁵ Pasha, "Sharia Boards face Scrutiny amid Financial Crisis".

⁴⁶⁶ Jamal Abbas Zaidi, "Shari‘a Harmonization, Regulation and Supervision" (paper presented at the AAOIFI-World Bank Islamic Banking and Finance Conference, Manama, 10/11/2008), p2..

⁴⁶⁷ See: El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p71; Firoozye, "Tawarruq: Shariah Risk or Banking Conundrum?".

⁴⁶⁸ Karen Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully," Dubai Media Inc, <http://www.emirates247.com/eb247/banking-finance/islamic-finance/islamic-finance-standardisation-needs-to-be-tackled-carefully-2009-10-25-1.18970>. accessed 15 June 2012

Another reason for promoting standardisation is that it saves cost and time for IIFS.⁴⁶⁹ Standardising popular contracts will minimise the need to wait for SSB approval, resolve the issue of the shortage of Shari‘ah scholars in some countries, and help save the cost of SSB services. These outcomes would eventually increase IIFS efficiency, reduce the overall transaction cost, and provide a level playing field for the Islamic finance industry to compete with its conventional counterpart.⁴⁷⁰

The current lack of uniformity in Shari‘ah rulings is also affecting the efficiency of the Islamic finance industry. For instance, in 2008, the Japan Bank for International Cooperation (JBIC) delayed its plan to issue *shukūk* after the SSBs at Citibank of Dubai and CIMB Malaysia, the two banks selected to structure the deal, gave conflicting views of the proposed structure’s Shari‘ah compliance.⁴⁷¹ To accommodate the two conflicting opinions, the issuance structure had to be based on the *mushārah* model rather than the originally proposed *murābahah* model. This lack of uniformity in SSB opinions increases cost, transaction time, and the issuer’s sensitivity to risk.

Another benefit of standardisation is boosting the international marketability of Shari‘ah-compliant products.⁴⁷² Currently, a product which is deemed Shari‘ah compliant in Malaysia, such as *bay‘ al-dyn* (the selling of debt), may not be accepted by GCC Shari‘ah scholars.⁴⁷³ Shari‘ah standardisation will mean that a product can be

⁴⁶⁹ Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK," p104.

⁴⁷⁰ Nidal Alsayed, "Shari‘ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance," *MPRA Paper*(2009) <http://mpa.ub.uni-muenchen.de/20204/> accessed 22 October 2010; Wafica Ali Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," *Review of Islamic Economics* 12, no. 2 (2008): p98; Zaidi, "Shari‘a Harmonization, Regulation and Supervision," p3.

⁴⁷¹ Yaacob, Muhammad, and Smolo, "International Convention For Islamic Finance: Towards Standardisation ". p21.

⁴⁷² Ghoul, "The Standardization Debate in Islamic Finance: A Case Study " p3.

⁴⁷³ Ibid.

approved in Dubai and marketed in Malaysia without confusion, uncertainty, and complication.⁴⁷⁴

In addition to improving the marketability of existing products, standardising basic contracts would motivate SSBs and the management of IIFS to introduce new products and services in order to compete with other players in the market.⁴⁷⁵ Ozgur Tanrikulu,⁴⁷⁶ speaking as the head of Islamic finance at McKinsey, a global management consulting firm, argued that innovation will only occur once the essentials are standardised, but that a market where the basics are frequently questioned will impede growth.

Moreover, supporters of standardisation argue that it will help to mitigate Shari'ah risk—that is, the risk that a contract can be deemed invalid and its enforceability thus called into question in both Muslim and secular countries. This is especially the case when Islamic parties' articles of association restrict them from signing a non-Shari'ah-compliant contract.⁴⁷⁷ In *Investment Dar v Blom Development Bank*,⁴⁷⁸ for example, the claimant defaulted on a \$100 million *ṣukūk* and argued in its legal defence that the contract in question was not Shari'ah-compliant, despite the fact its own Shari'ah board had approved it as such. Global rating agencies such as Moody's are concerned with such risk, as it may have an adverse impact on the assessment of credit risk.⁴⁷⁹

Finally, proponents of standardisation argue that standardising Shari'ah *fatwa* makes the task of regulators simple and fairly straightforward. Conflicting Shari'ah

⁴⁷⁴ Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance". p8.

⁴⁷⁵ Ibid., p16.

⁴⁷⁶ Robin Wigglesworth, "Sharia Boards: Scholars Hold Sway over The Success of Products," The Financial Times, <http://www.ft.com/cms/s/0/91c1636e-3836-11de-9211-00144feabdc0.html#axzz1y8yjhBuO>. accessed 18 June 2012

⁴⁷⁷ Djojogito, "Mitigating Legal Risk in Islamic Banking Operations."; Sole, "Introducing Islamic Banks into Conventional Banking Systems". p4.

⁴⁷⁸ *Investment Dar Co KSCC v Blom Developments Bank Sal.*

⁴⁷⁹ Howladar, "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance".

interpretations and practises make it difficult for regulators to oversee the industry and safeguard the public.⁴⁸⁰ With financial institutions utilising inconsistent *fatwas* to maximise their profit, it is difficult to ensure that clients are receiving value for the premium they have paid to protect their faith, given that Islamic financial products tend to be more expensive than conventional ones.⁴⁸¹ This uncertainty can make some countries reluctant to open their market to Shari‘ah-compliant products. Supervising a financial system with conflicting Shari‘ah models would be ineffective, costly, and unwieldy.⁴⁸² Without a semblance of consistency, it would be difficult to establish sound national and international compliance practises.

But with a Shari‘ah standard, financial institutions will be able to follow uncomplicated guidelines to ensure and report Shari‘ah compliance to stakeholders in a more consistent and transparent manner.⁴⁸³ It is the case, too, that standardisation helps regulators to design an adequate regulatory framework that suits the nature of Islamic finance. Paul M. Koster,⁴⁸⁴ the former CEO of Dubai Financial Services Authority (DFSA) stated in a speech at the 6th Summit of the Islamic Financial Services Board (IFSB) that standardisation is a serious challenge in Islamic finance domain. He argued that the issue is more problematic for non-Islamic regulators as—in the absence of an Islamic financial standard—they have to rely on conventional standards to inadequately address an issue unique to Islamic finance. This view is also

⁴⁸⁰ Alsayyed, "Shari‘ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance". p8; Yaacob, Muhammad, and Smolo, "International Convention For Islamic Finance: Towards Standardisation ". p33.

⁴⁸¹ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p290.

⁴⁸² Muhammad Syafii Antonio, "What is the Future Outlook of Shar‘iah Harmonization?" (paper presented at the (ISRA) Islamic Finance Seminar, Kuala Lumpur, 11/11/2008), p4..

⁴⁸³ Bilal Rasul, "Identifying the Main Regulatory Challenges for Islamic Finance," Bloomsbury Publishing, <http://www.qfinance.com/regulation-best-practice/identifying-the-main-regulatory-challenges-for-islamic-finance?full>. accessed 25 June 2012; Zaidi, "Shari‘a Harmonization, Regulation and Supervision," p1.

⁴⁸⁴ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

shared by John B. Taylor, the former Under Secretary of the United States Treasury for International Affairs. He stated that

The lack of uniformity of standards for Islamic banking practises across Islamic countries makes it difficult to apply the same prudential regulatory standards (e.g. capital adequacy requirements) across the board. This calls for more harmonization of Islamic banking practises, which in turn calls for harmonization of Shari‘ah standards at the national and international levels.⁴⁸⁵

4.3.2. Arguments against Standardisation

Despite the strong case advanced by proponents of standardisation, there are also equally passionate voices of resistance offering several reasons to justify their position. First, some experts do not see the lack of consistency as a serious issue. Ayub⁴⁸⁶ has suggested that standardisation is more of a “buzzword” than assumed substantive issue. He concedes that although a few issues emerged in the early days of the industry, most of these, he argues, have been dealt with by the scholarly works of Shari‘ah jurists. Similarly, Laldin⁴⁸⁷ holds that differences among SSB *fatwas* are exaggerated. He also believes that the practise of Islamic finance is becoming less controversial in the marketplace. Grais and Pellegrini⁴⁸⁸ refer to a study conducted by the General Council for Islamic Banks and Financial Institutions (CIBAFI) which suggests that there is a consensus in 90% of the Shari‘ah *fatwas*. According to Khan,⁴⁸⁹ a CEO at an international Islamic investment firm, the remaining conflicting *fatwas* give the industry room for innovation to design Shari‘ah-compliant products.

⁴⁸⁵ John B. Taylor, "Understanding and Supporting Islamic Finance: Product Differentiation and International Standards" (paper presented at the Islamic Finance: Current Legal and Regulatory Issues, Cambridge, 8 /5/ 2004), p3.

⁴⁸⁶ Ayub, *Understanding Islamic Finance*, p465.

⁴⁸⁷ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

⁴⁸⁸ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁴⁸⁹ Ghoul, "The Standardization Debate in Islamic Finance: A Case Study " p4.

In theory, most Shari‘ah *fatwas* exhibit either a consensus or an agreement on the principles of Islamic finance, such as the prohibition of *ribā* and *gharar*.⁴⁹⁰ However, the practise shows a fair degree of divergence in the application of such principles—for instance, whether or not a particular contract such as *‘inah* breaches the Islamic finance principle of prohibiting *ribā*. Because the CIBAFI study cited by Grais and Pellegrini is inaccessible—it has not been published and remains unavailable to the public⁴⁹¹— it is not possible to assess the credibility of its findings or its approach in collecting and analysing data, nor to verify the representative nature of its samples. Nevertheless, assuming that the study’s findings are accurate, one could well argue that the need for standardisation remains because most Shari‘ah-compliant products offered on the market are based on the 10% of disputed *fatwas*. For example, organised *tawarruq*, remains “the most used single liquidity providing scheme”⁴⁹² in the industry, notwithstanding the resolution of the International Council of Fiqh Academy on the prohibition of organised *tawarruq*. Similarly, a large proportion of Shari‘ah-compliant products are based on *murābahah* structure, which is disputed by some scholars.⁴⁹³ This should not be surprising, since the two structures (organised *tawarruq* and *murābahah*) share similarity with interest-based products and pose a small risk to IIFS.

⁴⁹⁰ See the discussion in chapters one and two.

⁴⁹¹ The researcher contacted CIBAFI on 21/6/2012 and 24/9/2012 enquiring about the study but did not receive any response.

⁴⁹² Firoozye, "Tawarruq: Shariah Risk or Banking Conundrum?"; see also: Nabil A Issa, "Beyond Tawarruq: Availability of Other Forms of Islamic Financing in Saudi Arabia," [Islamicfinancenews.com](http://www.kslaw.com/imageserver/KSPublic/library/publication/IslamicFinanceNewsNabilIssaOct2010.pdf), <http://www.kslaw.com/imageserver/KSPublic/library/publication/IslamicFinanceNewsNabilIssaOct2010.pdf>, accessed 20 June 2012

⁴⁹³ Firoozye, "Tawarruq: Shariah Risk or Banking Conundrum?"; ‘Amrū al-Sawādī, "Da‘awāt Ijād Muntajāt Islāmiyyah lil-Ta‘āmul ma‘ al-Qurūd al-Muta‘athrih", *al-Iqtiṣādiyyah*, 22 May 2011 http://www.aleqt.com/2011/05/22/article_540808.html, accessed 24 June 2012.

Opponents of standardisation also argue that it is against the diverse nature of Islam.⁴⁹⁴ Shari‘ah is not a ready-made law; instead, the sources of Shari‘ah provide general principles which are interpreted through the tool of *ijtihad* to understand the Islamic view on a certain transaction.⁴⁹⁵ *Ijtihad* has been a fundamental element of Shari‘ah law and has contributed for centuries to the richness of Islamic jurisprudence. It is what gives Shari‘ah the dynamic ability to survive and the capacity to be applicable to a given time and place. Conflicting opinions will always exist; there is no Pope in Islam, and Muslims are only bonded by Quran and *sunnah* (the primary sources of Shari‘ah) .⁴⁹⁶ Therefore, opponents argue, it is not appropriate to have an international body to distinguish the “right” interpretation from the “wrong” one.⁴⁹⁷

Besides, a regulatory enforcement of one Shari‘ah interpretation over others might not be accepted by Muslim societies subscribing to various schools of thought, whether in one or multiple countries.⁴⁹⁸ Moreover, such enforcement might not suit institutions which operate in varied circumstances either on the domestic or global level. For instance, a Shari‘ah *fatwa* issued by SSBs in a fully flagged Islamic bank might be difficult to implement in a conventional bank with Islamic windows, or in a conventional bank in the process of converting into an Islamic bank.

Furthermore, opponents of standardisation argue that it would slow down innovation and hinder the development of new products. Currently, the industry is said to be taking advantage of the conflicts in *fatwas* to increase its share of the

⁴⁹⁴ Alsayed, "Shari‘ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance"; Zaidi, "Shari‘a Harmonization, Regulation and Supervision."

⁴⁹⁵ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

⁴⁹⁶ Ibid.; Zaidi, "Shari‘a Harmonization, Regulation and Supervision," p3.

⁴⁹⁷ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

⁴⁹⁸ Zaidi, "Shari‘a Harmonization, Regulation and Supervision," p3., Chris Wright, "The Shariah Scholar Cartel," Asiamoney, <http://www.chriswrightmedia.com/asiamoney-sep06-shariahscholars/>. accessed 20 April 2011, 1-3.

growth in the global market.⁴⁹⁹ Salman Younis,⁵⁰⁰ the former managing director of Kuwait Finance House (Malaysia), suggests that “there are issues on Shari‘ah interpretation, but they are not a hurdle to the growth of Islamic banking. In fact, we firmly believe that if you have Shari‘ah harmonization, it may kill innovation”. Moreover, lack of consistency can be good for business in the sense that it allows financial institutions to introduce various products directed to specific consumers or markets.⁵⁰¹

However, it is doubtful whether standardisation would actually hinder innovation, considering that standardisation has been a feature of conventional finance for many decades without slowing down financial engineering. There is no restriction on introducing new products to the market after receiving approval of the regulatory body or the central Shari‘ah supervisory board. In fact, as mentioned earlier, proponents of standardisation argue that it would boost development and create an incentive for financial institutions to focus on innovation to be able to compete in the market. Admittedly, enforcing a standard might have an impact on the speed of approving new innovative products,⁵⁰² but protecting the market from Shari‘ah arbitrage and maintaining stakeholder’s confidence justifies such delay.

A final strong argument put forward by opponents of standardisation is that setting international Shari‘ah standards is impractical because compliance with such standards could not be enforced or supervised unless the standards were imposed by national regulators.⁵⁰³ For example, the standard of the Accounting and Auditing

⁴⁹⁹ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p286.

⁵⁰⁰ Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p98.

⁵⁰¹ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

⁵⁰² Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p99.

⁵⁰³ Oxford Analytica, "Islamic Finance Moves Toward Common Standards," Oxford Analytica, http://www.forbes.com/2010/03/08/islam-finance-sharia-business-oxford-analytica_2.html. accessed 23 May 2012; Ghoul, "The Standardization Debate in Islamic Finance: A Case Study".

Organisation for Islamic Financial Institutions (AAOIFI) is approved by Shari‘ah scholars from different schools of thought and sects. However, in practise, few countries enforce it on the national level. What the industry needs is to regulate the implementation of existing AAOIFI standards, rather than to establish new standards.⁵⁰⁴ Nonetheless, the experience of AAOIFI and the limited implementation of its standards do not subdue the need for standardisation and the long-term harm that is likely to occur in its absence. Rather, the situation should encourage an examination of why AAOIFI standards were not effective and of better alternative remedies, an issue which is further discussed in Part 4.5 of this chapter.

4.4. Causes of Juristic Differences

To resolve the issue of inconsistency in SSB *fatwas*, it would be useful to understand the causes of such disagreements in the first place. However, it is important to emphasise that conflicts do not occur in the fundamental principles of Shari‘ah, but rather in the secondary issues.⁵⁰⁵ For instance, there is no dispute with regard to the faith, i.e., the unity of Allah, the prophecy of Muhammad, and the authenticity of the Quran. There is also no major divergence in how the five pillars of Islam, such as the five daily prayers, fasting, and pilgrimage, are performed. Differences mainly occur in applying some of the Shari‘ah principles to certain cases.⁵⁰⁶

Islamic law has not been received as ready-made rules for implementation.⁵⁰⁷ Unlike modern laws, in which interpretation is not always required,⁵⁰⁸ in Shari‘ah,

⁵⁰⁴ Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

⁵⁰⁵ ‘AbdAllāh al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā*, 3rd ed. (Resalah Publishers, 2010), p12; Mohd Daud Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory" (PhD thesis, University of St. Andrews, 1993), p89.

⁵⁰⁶ "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p89.

⁵⁰⁷ Bernard Weiss, "Interpretation in Islamic Law: The Theory of Ijtihad," *The American Journal of Comparative Law* 26, no. 2 (1978): p199.

interpretation of its sources is necessary to understand the intention of the Lawgiver. If the sources of Shari‘ah were self-evident, there would be no need for interpretation, because they would be the law itself rather than its sources.⁵⁰⁹ The interpretation process does not have a speculative nature, but is rather governed by a well-stated approach and methodical tool known as *ijtihād*, which a jurist uses to extract the law on a given matter.⁵¹⁰ Hallaq⁵¹¹ defines *ijtihād* as “the maximum effort expended by the jurist to master and apply the principles and rules of *usul al-fiqh* (legal theories) for the purpose of discovering God’s law”. Similarly, Baker⁵¹² quotes a definition of *ijtihād* provided by al-Amidī (d.631 AH/1233 CE) which indicates that the scholar’s *ijtihād* or conclusion of his interpretation shall be deemed void if he neglects to employ his scholarly skill to find out evidence which he was competent to discover. Interpretations can take the form of a *fatwa*, a judge’s decision, or a commentary on the Quran or *sunnah*.⁵¹³ Accordingly, because *ijtihād* is in essence an interpretive process, it will indirectly lead to conflicting opinions among Shari‘ah scholars.⁵¹⁴

The science of *fiqh* (Islamic jurisprudence) has been built on attempts at practising *ijtihād*.⁵¹⁵ The practise of *ijtihād* began during the Prophet’s life, while he was able to approve or reject the conclusion of any *ijtihād*.⁵¹⁶ Therefore, at this stage, *ijtihād* did not create any diversity in the Islamic society.⁵¹⁷ However, after the death of the

⁵⁰⁸ Mohd Daud Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," in *Islamic Finance: Innovation and Growth*, ed. Simon Archer and Rifaat Ahmed Abdel Karim (London: Euromoney Books and AAOIFI, 2002), p83.

⁵⁰⁹ Weiss, "Interpretation in Islamic Law: The Theory of Ijtihad," p203.

⁵¹⁰ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p82; Weiss, "Interpretation in Islamic Law: The Theory of Ijtihad," p202.

⁵¹¹ Wael B. Hallaq, "Was the Gate of Ijtihad Closed?," *International Journal of Middle East Studies* 16, no. 1 (1984).

⁵¹² Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p83.

⁵¹³ Ibid.

⁵¹⁴ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p291.

⁵¹⁵ Ibid.

⁵¹⁶ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p22.

⁵¹⁷ 'Alī al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā'*, 2nd ed. (Dār al-Fikr al-'Arabī, 1996), p18.

Prophet, his companions and Shari‘ah scholars after them were challenged with unprecedented cases in different circumstances and had to exercise *ijtihād* to arrive at a legal conclusion.⁵¹⁸ As the Prophet was not alive to approve or reject conclusions, various judgments have existed based on different methodologies and legal arguments.⁵¹⁹

However, before proceeding to the causes of jurists’ disagreements, a brief reminder is warranted about the difference between Shari‘ah and Islamic jurisprudence, commonly called “*fiqh*”.⁵²⁰ As discussed in chapter one, Islamic jurisprudence is a subset of Shari‘ah, composing a single area of the broader concept. Shari‘ah serves as the basis of all principles formed and expanded under *fiqh*, whereas the term “Islamic jurisprudence” generally refers to scholarly comprehension and findings derived from the primary and secondary sources of Shari‘ah. In this respect, Shari‘ah is a divine law, whereas *fiqh* is a human interpretation of these divine sources to arrive at God’s law in a specific case.⁵²¹ In other words, a *fatwa* issued by a Shari‘ah scholar is not deemed entirely definitive; it is rather a personal statement of what the *mujtahid* believes to be the intention of the Lawgiver.⁵²²

Reading the legal history of Islamic jurisprudence informs us about many causes of disagreements between Shari‘ah jurists. Several attempts have been made in classical and contemporary literature to explain and classify the causes of

⁵¹⁸ See: Nazeem MI Goolam, "Ijtihad and Its Significance for Islamic Legal Interpretation " *Michigan State Law Review* 2006, no. 6 (2006): p1446; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā*’, p23.

⁵¹⁹ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p291; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā*’, p22.

⁵²⁰ Abdulrahman Baamir and Ilias Bantekas, "Saudi Law as Lex Arbitri: Evaluation of Saudi Arbitration Law and Judicial Practice," *Arbitration International* 25, no. 2 (2009).

⁵²¹ Weiss, "Interpretation in Islamic Law: The Theory of Ijtihad," p203; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p88.

⁵²² "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p87.

disagreement between Shari‘ah scholars.⁵²³ This section discusses the most common reasons which are believed to have a major impact on the inconsistency of *fiqh*.

4.4.1. Variable Quranic Recitations

Some verses of the Quran can be recited in two linguistically acceptable ways. These two readings sometimes result in two different meanings.⁵²⁴ One commonly cited example is the following verse: “O you who believe! When you intend to offer As-Salat [the prayer], wash your faces and your hands [forearms] up to the elbows, rub [by passing wet hands over] your heads, and [wash] your feet up to ankles”.⁵²⁵ The issue in this example is whether the feet should be washed or wiped to validate *wuḍū’* (ablution). There are two grammatical possibilities for the word “feet” in the original Arabic text. One reads the word as accusative (*wa arjulakum*), which indicates that the feet should be washed along with the face and the hands. The second reading of the word pronounces it as a genitive (*wa arjulikum*), which requires only wiping the feet, as is the case with the head.⁵²⁶ The majority of scholars, including the four *sunni* schools of thought, uphold the first reading, which makes washing the feet obligatory in ablution. The *shī‘ah imāmiyyah* school of thought adopts the second

⁵²³ See for example: Aḥmad Ibn Taymiyah, *Raf‘ al-Malāam ‘an al-A‘imah al-A‘lāam* (The General Presidency of Scholarly Research and Ifta, 1993); al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā’*, p29; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā’*, p27; Ahmad Zaki Hammad, *Islamic Law: Understanding Juristic Differences* (Indianapolis: American Trust Publications, 1992), p28; Abu Ameenah Bilaal Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, ed. Bradley Philips, 3rd ed. (Riyadh: International Islamic Publishing House, 2006), p121; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p63; Muhammad Salih Uthaymin, *Differences of Opinion Amongst The Scholars: Their Causes and our Position Towards Them*, trans. Abu Safwan Farid Haibatan (Birmingham, U.K.: al-Hidaayah Pub. and Distribution, 1997); Muṣṭafā al-Khin, *Athar al-Akhtilāaf fī al-Qawā‘id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā’*, 7th ed. (Resalah Publishers, 1998), p35.

⁵²⁴ Hammad, *Islamic Law: Understanding Juristic Differences*, p31; Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p125.

⁵²⁵ Taqī al-Din Hilali and Muhammad Muhsin Khan, "The Noble Quran," Muslim Directory, <http://quran.com/5/6>. accessed 2 July 2012.

⁵²⁶ Hammad, *Islamic Law: Understanding Juristic Differences*, p31; Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p125., Ismā‘īl Shandī and Taqīal-Dan ‘abd al-bāsīt, "al-Qirā‘āt al-Qur‘āniyyih wa Atharuhā fī Akhtil-āaf al-Fuqahā’," *Majallah Jāmi‘ah al-Quds al-Maḥḥah lil-‘bḥāth wa al-Dirāsāt*, no. 8 (2006): p316; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p64; al-Khin, *Athar al-Akhtilāaf fī al-Qawā‘id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā’*, p38.

reading, which deems wiping the feet as sufficient to validate the ablution.⁵²⁷ The majority position is supported by the recorded regular practise of the Prophet of washing his feet when performing ablution.⁵²⁸

4.4.2. *Using Words with Multiple Meanings*

Disagreement between jurists can occur because of the use of *mushtarak* words in Shari‘ah sources.⁵²⁹ The term *mushtarak* literally means “homonymous” or “semantically ambiguous”.⁵³⁰ A *mushtarak* word or sentence can have two or more equivalent meanings. It can also take place in the Quran and the *sunnah* with no direct clarification by the Lawgiver. Differences among Shari‘ah scholars arise when they try to establish the exact meaning of these words.⁵³¹ One example of a *mushtarak* word which resulted in two different jurisprudential opinions is the word *qurū’* (time) used in the Quranic verse 2:228. The verse reads, “Divorced women remain in waiting for three *qurū’*”.⁵³² According to the verse, divorced women cannot remarry other men before the passing of three *qurū’*. Linguists and Shari‘ah scholars agree that the word *qur’*, which is the singular of the word *qurū’* mentioned in the verse, means “time”. However, they dispute whether ‘time’ here applies to “menstruation or to the period between two menstruations”.⁵³³ Both meanings have valid origins in Arabic. The jurisprudential impact of this dispute is that in the view of the Ḥanafī and Ḥanbalī schools of thought, women have to wait three periods of menstruation before remarrying, while in the Mālikī and Shāfi‘ī schools of thought, they are required to

⁵²⁷ Hammad, *Islamic Law: Understanding Juristic Differences*, p31; Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p125.; Shandī and ‘abd al-bāsīt, "al-Qirā’āt al-Qur’āniyyih wa Atharuhā fī Akhtil-āaf al-Fuqahā’," p316; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p64.

⁵²⁸ Hammad, *Islamic Law: Understanding Juristic Differences*, p32; al-Khin, *Athar al-Akhtilāaf fī al-Qawā’id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā’*, p41.

⁵²⁹ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā’*, p96.

⁵³⁰ Hammad, *Islamic Law: Understanding Juristic Differences*, p19.

⁵³¹ al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā’*, p107; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā’*, p196.

⁵³² Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

⁵³³ Hammad, *Islamic Law: Understanding Juristic Differences*, p29. ; al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā’*, p107.

wait three periods of purity. The waiting period in the latter view is shorter than in the former.⁵³⁴ To make their decision, jurists had to rely on other evidence and texts to determine the Lawgiver's intention in using the word *qurū* ' in this specific verse. This is due to the fact that a *mushtarak* word presents two equivalent meanings that can be understood from a single word, and it is difficult to select the intended meaning without any external evidence.⁵³⁵

4.4.3. *Lack of Knowledge of Ḥadīth*

Despite the fact that *sunnah*⁵³⁶ is the second main source of Islamic law, and Muslims are obligated to follow it, a large part of the disagreement in Islamic jurisprudence is caused by issues related to *sunnah*.⁵³⁷ A jurist can take a position that is different from that of other scholars because he lacks knowledge of a particular tradition concerning the case in question.⁵³⁸ This happened to the companions of the Prophet after his death. They had different levels of familiarity with the prophetic *ḥadīth*, since some of the companions had been busy with other things such as business or farming or had enrolled in the army.⁵³⁹ In addition, the companions of the Prophet settled in different regions of the Islamic empire, and different schools of thought were established prior to the authoring of comprehensive collections of

⁵³⁴ al-Khin, *Athar al-Akhtilāf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āf al-Fuqahā* ', p78.

⁵³⁵ Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p68; al-Turkī, *Asbāb Akhtil-āf al-Fuqahā* ', p196; Hammad, *Islamic Law: Understanding Juristic Differences*, p29.

⁵³⁶ The expression *sunnah* means the accumulation of the teachings of Prophet Muhammad, which includes his sayings, actions, decisions, and his implicit approbation or disapproval of things. I have used *sunnah* and *ḥadīth* as synonyms. Other researchers draw a theoretical distinction between the two words. See: Muhammad Zubair Siddiqi, *Hadith Literature : Its Origin, Development and Special Features* (Cambridge: Islamic Texts Society, 1993), p2; Kamali, *Principles of Islamic Jurisprudence*, p58.

⁵³⁷ Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p71.

⁵³⁸ Hammad, *Islamic Law: Understanding Juristic Differences*, p36; Uthaymin, *Differences of Opinion Amongst The Scholars: Their Causes and our Position Towards Them*, p18; Ibn Taymiyah, *Raf' al-Malām 'an al-A'imah al-A'lām*, p9.

⁵³⁹ al-Turkī, *Asbāb Akhtil-āf al-Fuqahā* ', p25.

ḥadīth.⁵⁴⁰ In fact, the most famous collections of the *ḥadīth* only became available in the last part of the ninth century and the first half of the tenth century, whereas the founders of the four major schools of thought lived between the middle of eighth century and the first part of the ninth century.⁵⁴¹

According to Ibn Taymiyyah (d.728/1328),⁵⁴² even some of the eminent companions had no comprehensive knowledge of the Prophet's *ḥadīth*, and they issued *fatwas* that conflicted with a *ḥadīth* which they didn't know at the time. For instance, in the case of *'iddah* (a waiting period for women after the death of their husbands), verse 2:234 states, "And those of you who die and leave wives behind them, they [the wives] shall wait [as regards their marriage] for four months and ten days".⁵⁴³ However, verse 65:4 reads, "And for those who are pregnant [whether they are divorced or their husbands are dead], their *'iddah* [prescribed waiting period] is until they deliver [their burdens]".⁵⁴⁴ To conciliate between the two verses, two companions, 'Alī Ibn Abī Ṭālib and Ibn 'Abbās, held the view that if a husband passes away while his wife is pregnant, the wife has to wait for the longer of the two *'iddah* (four months and ten days or until giving birth).⁵⁴⁵ On the other hand, the majority of the companions and Shari'ah scholars held the view that the *'iddah* of a pregnant wife in this situation ends when she gives birth to her baby.⁵⁴⁶ The basis of this view is a *ḥadīth* reported by Al-Bukhārī: "Subai'a Al-Aslamiya gave birth to a child a few days after the death of her husband. She came to the Prophet and asked

⁵⁴⁰ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p126; Hammad, *Islamic Law: Understanding Juristic Differences*, p38.

⁵⁴¹ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p126; Ibn Taymiyah, *Raf' al-Malāam 'an al-A'imah al-A'lāam*, p17.

⁵⁴² *Raf' al-Malāam 'an al-A'imah al-A'lāam*, p10.

⁵⁴³ Hilali and Khan, "The Noble Quran".

⁵⁴⁴ *Ibid*.

⁵⁴⁵ al-Khin, *Athar al-Akhtilāaf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*, p48; Uthaymin, *Differences of Opinion Amongst The Scholars: Their Causes and our Position Towards Them*, p18.

⁵⁴⁶ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p271; al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā'*, p31.

permission to remarry, and the Prophet gave her permission, and she got married”⁵⁴⁷.

In this instance where the minority opinion conflicts with a prophetic *ḥadīth*, the disagreement between the minority and majority opinions stemmed from the minority not knowing that this *ḥadīth* existed.⁵⁴⁸ Moreover, in some situations, differences arise because one of the scholars relies on a weak (inauthentic) *ḥadīth* to justify his *fatwa*.⁵⁴⁹ This happens because not all jurists are specialists in the science of *ḥadīth*, a field of study that enables a scholar to examine the authenticity of a prophetic *ḥadīth*.

Nevertheless, Hammad points out that in the present day, the lack of knowledge of *ḥadīth* should not be used to justify a particular jurisprudential view, since nearly all *ḥadīth* collections are available to scholars. Technological advancements make it easy for jurists to search the collection of *ḥadīth* and investigate their authenticity before issuing a *fatwa*.⁵⁵⁰

4.4.4. Different Requirements for Adopting Ḥadīth

As mentioned earlier, issues related to the second source of Shari‘ah, the *sunnah*, have led to many conflicting opinions within Islamic jurisprudence. Unlike the Quran, some jurists dispute the authenticity of some of the reported *sunnah*.⁵⁵¹ *Ḥadīth* can be classified into two types, each defined by the number of people who reported a *ḥadīth* at every level of the chain of transmission: *mutawātir* (consecutive) and *aḥād* (single).⁵⁵² The former include *ḥadīth* that have been transmitted by a majority of people, which makes errors in what they narrated very rare. The latter include *ḥadīth* narrated by fewer people at each level of the chain of transmission. *Aḥād* forms the

⁵⁴⁷ al-Bukhārī, "Ṣaḥīḥ al-Bukhārī".

⁵⁴⁸ Ibn Taymiyah, *Raf‘ al-Malāam ‘an al-A‘imāh al-A‘lām*, p16; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p73.

⁵⁴⁹ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p127.

⁵⁵⁰ Hammad, *Islamic Law: Understanding Juristic Differences*, p39.

⁵⁵¹ al-Khin, *Athar al-Akhtilāaf fī al-Qawā‘id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā’*, p53; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā’*, p114.

⁵⁵² See: Kamali, *Principles of Islamic Jurisprudence*, p93; Hallaq, *An introduction to Islamic law*, p17.

majority of the prophetic *ḥadīth*. It is also unanimously deemed as speculative (*ẓanni*) in its chain of transmission, in its interpretation, or in both.⁵⁵³

For this reason, and to examine the authenticity of such tradition, each school of thought has certain requirements which this type of *ḥadīth* should meet before it can be accepted. For example,⁵⁵⁴ to accept an *āḥād ḥadīth*, Ḥanafī School requires the practise of the narrator to be in line with his narration (e.g., the way he performs a prayer should match his narration describing the performance of the prayer).⁵⁵⁵ In addition, if the subject of the tradition is one which concerned a majority of people, it should be reported by a large number of narrators. This is because if the *ḥadīth* were authentic, it would not fail to be narrated by many people.⁵⁵⁶ Moreover, unless the narrator was a jurist (*faqīh*), the *ḥadīth* would not be accepted if it were found to be in conflict with analogy (*qiyās*).⁵⁵⁷

The legal views which Ḥanafī concluded based on this rule are sometimes inconsistent with the views of other schools of thought who do not approve Ḥanafī's rules for examining the reliability of *āḥād ḥadīth*. Nevertheless, this does not mean that other schools of thought do not have their own requirements for accepting *āḥād ḥadīth*. For instance, the Mālikī School rejects this type of *ḥadīth* if it is found to be inconsistent with the established practise of the people of Medina (*'amal ahl al-Madīnah*).⁵⁵⁸ The latter is given priority over the former because the practises in Medina are deemed as a continuous tradition narrated by generations from the time of

⁵⁵³ While the transmission of *mutawātir* is deemed definitive (*qaṭ'ī*), its meaning can be open to more than one interpretation. See: Kamali, *Principles of Islamic Jurisprudence*, p79 & p96.

⁵⁵⁴ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p128.; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p77.

⁵⁵⁵ See: al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā'*, p79; al-Khin, *Athar al-Akhtilāaf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*, p436; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p78.

⁵⁵⁶ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p121.

⁵⁵⁷ al-Khin, *Athar al-Akhtilāaf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*, p426.

⁵⁵⁸ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p128.

the Prophet up until the time of the School's founder, Mālik Ibn Anas (d.179/795).⁵⁵⁹

As the examples above demonstrate, these various conditions naturally lead to conflicting legal conclusions.

4.4.5. *Adopting Certain Legal Principles*

Different schools of thought have adopted various principles and rules into their legal theory of how to interpret the original sources of the law. The aim of these theories was to ensure that legal arguments have a solid ground and sound reasoning. For example, according to the Ḥanafī School, the generality of Quranic verse is not to be restricted by an *āḥād ḥadīth*.⁵⁶⁰ On the basis of this principle, the Ḥanafī School does not accept a *ḥadīth* which allows, in the absence of two witnesses, the testimony of one witness in addition to the plaintiff oath.⁵⁶¹ The school deemed this allowance to conflict with the minimum requirements of testimony set by the Quranic verse (two men or one man and two women).⁵⁶² Similarly, the Ḥanbalī School has its own special principles to establish law. One of these is that, in legal consideration, it favours a weak *ḥadīth* over a merely human reasoning. Aḥmad Ibn Ḥanbal, the School's founder, states that he prefers a weak *ḥadīth* over a man's opinions.⁵⁶³ Some scholars do not agree with that; they see no authority for such a *ḥadīth*, since it is not authentic. Nevertheless, this diversity of approaches towards establishing a law is bound to result in different juristic opinions.

⁵⁵⁹ Aisha Bewley, "The 'Amal of Madina," www.bewley.virtualave.net, <http://bewley.virtualave.net/amalmadina.html>. accessed 10 August 2012. For more extensive study about this issue see: Ḥassān Filimbān, *Khābar al-Wāḥid Idhā Khālaf 'Amal ahl al-Madīnah* (Dār al-Buḥūth lil-Dirāsāt al-Islāmiyah Wa Iḥyā al-Turāth, 2000).

⁵⁶⁰ Philips, *Evolution of Fiqh : Islamic Law and the Madh-habs*, p130; al-Khin, *Athar al-Akhtilāf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*, p117.

⁵⁶¹ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p119; al-Khin, *Athar al-Akhtilāf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*, p443.

⁵⁶² Hilali and Khan, "The Noble Quran".

⁵⁶³ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p133.

The adoption of different views in regard to the hierarchical order of the authority of legal sources of Shari‘ah has further contributed to the disagreements in Islamic jurisprudence.⁵⁶⁴ It is unanimously agreed that the Quran is the highest source in terms of authority, followed by the *sunnah*. However, most of the disputes occur in the rank of the secondary sources, as there is no uncontested standard to determine which one of these should have priority over the other. Instead, some jurists give priority to sources which support their particular view.⁵⁶⁵ According to Baker,⁵⁶⁶ Al-Shafi‘i, in his book *al-Risālah*, regarded by some researchers as the first book written in Islamic legal theory, argues that a lot of jurisprudential conflicts were caused by not following a systemic method in dealing with Shari‘ah sources to justify a legal view. Al-Shafi‘i believes that legal decisions should be grounded on the following sources: Quran, *sunnah*, *ijmā‘* (consensus), and *qiyās* (analogy), in that order.⁵⁶⁷ He criticises many of his predecessors and contemporary jurists for basing their jurisprudential views on a lower level of Shari‘ah sources rather than a higher one. However, Al-Shafi‘i’s ideal proposal does not work in practise as it looks in theory.⁵⁶⁸ Some of his School followers, not to mention his opponents, do not observe his theory. In fact, Baker argues that Al-Shafi‘i himself was not consistent in applying his own theory.⁵⁶⁹

While some legal sources and principles are accepted by most schools of thought, each school can have its own definitions, interpretations, view of authority, and limit of application of each source or principle.⁵⁷⁰ For instance, while all schools agree on the definition of the Quran, disagreements arise on issues relating to the secondary

⁵⁶⁴ Muhammad Khalid Masud, "Ikhtilaf al-Fuqaha: Diversity in "Fiqh" as a Social Construction," Musawah, <http://www.musawah.org/sites/default/files/WANTED-EN-2edition.pdf>. accessed 10 October 2012; al-Khafif, *Asbāb Akhtil-āaf al-Fuqahā‘*, p194.

⁵⁶⁵ Masud, "Ikhtilaf al-Fuqaha: Diversity in "Fiqh" as a Social Construction" p76; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p73.

⁵⁶⁶ "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p74.

⁵⁶⁷ Masud, "Ikhtilaf al-Fuqaha: Diversity in "Fiqh" as a Social Construction" p76.

⁵⁶⁸ Hallaq, *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*, p18.

⁵⁶⁹ Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p74.

⁵⁷⁰ See: *ibid.*, p84; al-Khafif, *Asbāb Akhtil-āaf al-Fuqahā‘*, p209.

sources of law such as *ijmā'* (consensus), *qiyās* (analogy), *Istihsān* (juristic preference),⁵⁷¹ *istiṣhāb* (assumption of permanence of past conditions in a present situation),⁵⁷² *urf* (custom), *maṣlaḥah* (protecting the public interest), *qawl- al-sahābī* (interpretation or the *fatwa* of the companion of the Prophet), and *sadd al-dhariā'i* (precautionary legal prohibition).⁵⁷³ These differences in the legal theories of schools result in conflicting legal conclusions. One example is the Zāhirī School's refusal to use analogy as a source of law, although it is accepted by the other major schools of thought.⁵⁷⁴ This had led to the Zāhirī School's refusal to extend the scope of *ribā* (usury) beyond that explicitly stated in the letter of the law.⁵⁷⁵

4.4.6. *Disregarding the Change of Maṣlaḥah*

One of the behaviours which widened disagreements in Islamic jurisprudence is ignoring the underlying purpose of jurisprudential rulings.⁵⁷⁶ Many Shari'ah theorists such as Ibn al-Qayyim (d.751/1350) and al-Shāṭibī (d.790/1388) have stated that Shari'ah rulings are established to serve the human interest in this world and in the hereafter.⁵⁷⁷ Accordingly, some rules can change when the underlying cause on which they were founded is absent or no longer active. As a major part of jurisprudence is based on *maṣlaḥah* (public interest) and causes which are influenced by certain changeable elements such as custom and circumstances, many jurists change their

⁵⁷¹ R Paret, "Istihsān and Istiṣlāḥ" in *Encyclopaedia of Islam* (Brill Online, 2012) <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/istihsan-and-istishlah-COM_0395> accessed 10 October 2012.

⁵⁷² Y Linant de Bellefonds, "Istiṣhāb" ibid. <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/istishab-SIM_3692> accessed 10 September 2012.

⁵⁷³ Literally "the blocking of means"; the blocking of actions that could lead to unlawful ends. See: Kamali, *Principles of Islamic Jurisprudence*, p397. For more about juristic differences related to secondary sources, see: al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā'*, p193; al-Khin, *Athar al-Akhtilāaf fi al-Qawā'id al-Uṣūliyyah fi Akhtil-āaf al-Fuqahā'*, p529; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p144-87.

⁵⁷⁴ al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā'*, p205; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā'*, p151.

⁵⁷⁵ al-Khin, *Athar al-Akhtilāaf fi al-Qawā'id al-Uṣūliyyah fi Akhtil-āaf al-Fuqahā'*, p483.

⁵⁷⁶ Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p85.

⁵⁷⁷ Ibid.

fatwas when the previous ruling no longer serves the welfare of the public.⁵⁷⁸ This can happen to one jurist at different stages of his life or to different scholars in different places or times. For example, when al-Shāfi‘ī relocated from Iraq to Egypt, he changed some of his *ijtihād* following the needs and the circumstances of the Egyptian society.⁵⁷⁹ These different views are known within the Shāfi‘ī school as “the old opinion” and “the new opinion”, and both form the jurisprudence of the Shāfi‘ī school.⁵⁸⁰ He had different students in both countries who spread his teaching across the world.

Another example comes from the Ḥanafī school. While Abū Hanīfah generally accepted testimonies of two witnesses with *‘adālah* (upright character), his two renowned students, Abū Yūsuf (d.182/798) and Muḥammad Ibn al-Ḥasan al-Shaybāny (d.189/805), did not accept any testimony in court unless each witness was accredited by a trustworthy person (*tazkiyah*).⁵⁸¹ This is because unlike in the time of Abū Hanīfah, such inquiry was deemed necessary in their era to protect the public interest. Eventually, all these conflicting legal opinions became part of the wider Islamic jurisprudence.⁵⁸²

In more contemporary times, the *fatwas* of a Shari‘ah scholar can be influenced by the society where he lives. For instance, it is said that Malaysia’s Shari‘ah rulings tend to be moderate because the community is formed of different races and religions.⁵⁸³

⁵⁷⁸ al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā’*, p242.

⁵⁷⁹ Muḥamad al-Rustāqī, *al-Qadīm wa al-Jadīd Min Madhhab al-Imām al-Shāfi‘ī* (Dār Ibn Ḥazm 2005).

⁵⁸⁰ It is worth noting that some researcher strongly dispute that the change of Shāfi‘ī view was influenced by the Egyptian custom and social environment. See: Limin Naji, *Daḥḍ Maqālah Ta`thunr Fiqh al-Imām al-Shāfi‘ī bi-āl-Bī`ih al-Maṣriyyh* (al-Mansurah: Dar al-Kalimah, 2012).

⁵⁸¹ al-Khafīf, *Asbāb Akhtil-āaf al-Fuqahā’*, p245.

⁵⁸² Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p86.

⁵⁸³ Mohd Shahrulnizam Abd Hamid, "Shariah Interpretation Inconsistencies in Takaful Operation," *INCEIF*,

http://www.academia.edu/399303/Inconsistencies_in_Shariah_Interpretations_The_Takaful_Experience accessed 10 July 2012.

4.4.7. *The Structure of the Fatwa Question*

The way in which the fatwa question is presented can cause disagreement.⁵⁸⁴ This is because a *fatwa* is a religious response to an inquiry voluntarily put forward by an individual or by an IIFS about the permissibility of certain contracts. Scholars will answer according to the information presented in the question, which is controlled, to some extent, by the inquirer, who can choose what details to reveal in the question and how to present it. It is claimed⁵⁸⁵ that some institutions present the *fatwa* question in a way that guarantees its permissibility. Normally, scholars start their answer by stating that if the contract is structured as presented in the question, then it is permissible. The outcome of the *fatwa* is then reported later without the question, and the IIFS states that its product is approved as Shari'ah compliant. However, other scholars who are specialists in the field of Islamic finance and aware of the real implementation of such contracts in the market might issue a *fatwa* in conflict with the *fatwa* provided by the first Shari'ah scholar.⁵⁸⁶ The inconsistency in this case is not caused by a difference in legal principles; rather, it is a result of the lack of an institutionalised process of issuing *fatwas* which takes into account the full context of the *fatwa* as well as the impact of the *fatwa* on public policy.⁵⁸⁷

As the foregoing discussion shows, some causes of juristic disagreement such as variable Quranic recitations and linguistic vagueness are inevitable, since they are

⁵⁸⁴ Walid Hegaz, "Fatwas and the Fate of Islamic Finance: A Critique of the Practice of Fatwa in Contemporary Islamic Financial Markets " in *Islamic Finance: Current Legal and Regulatory Issues*, ed. Nazim Ali (Islamic Finance Project, Islamic Studies Program, Harvard Law School., 2005), p141.

⁵⁸⁵ See: Siti Faridah Abd Jabbar, "The Governance of Shari'a Advisers of Islamic Financial Institutions: The Practice in Malaysia," *The Company Lawyer* 30, no. 10 (2009): p313; 'Izz al-Dīn Zighībah "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Hūlūl Muqtarahah " (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31 /5/ 2009), p24.

⁵⁸⁶ See an example in El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p33.

⁵⁸⁷ See generally: Hegaz, "Fatwas and the Fate of Islamic Finance: A Critique of the Practice of Fatwa in Contemporary Islamic Financial Markets " p141.

relatively outside of human control.⁵⁸⁸ They are natural causes in the sense that they are not affected by any particular mindset in Islamic legal theory. Other causes of disagreement, such as the adoption of certain legal principles, are generally human-made, and are said to cause most of the disagreements in Islamic jurisprudence.⁵⁸⁹ Since the basis of these legal theories is human intellect, they can be speculative and relative. It is natural for people to have different levels of competency to understand legal texts and the issues associated with them. When two opinions of Islamic jurisprudence seem to conflict, it shows that one of the legal sources which was the basis of the conflicting view has been wrongly understood or implemented.⁵⁹⁰ Human reasoning is imperfect; hence it is the responsibility of later jurists to identify the fault in earlier arguments, and to choose their preference after putting much effort into carefully considering the evidence behind the two opinions.

4.5. Remedies for Inconsistency

With the causes of disagreements between Shari‘ah scholars addressed, this section investigates how classical and contemporary jurists have dealt with this issue. It suggests potential remedies and highlights the limitations of implementing them in Islamic and secular countries. As the earlier discussion attests, conflicts in Islamic jurisprudence have taken place in the past and will continue to do so.⁵⁹¹ Nevertheless, Islamic rulers and Shari‘ah theorists offer various mechanisms to tackle the issue of inconsistent *fatwas* from a juristic or an administrative point of view or from both.

With regard to the juristic remedies, first, conflicting opinions in Islamic jurisprudence can be reconciled by using a tool known in Islamic legal theory as *al-*

⁵⁸⁸ Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p63.

⁵⁸⁹ al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā*, p266.

⁵⁹⁰ al-Khin, *Athar al-Akhtilāaf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā*, p97; Bakar, "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory," p89.

⁵⁹¹ "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p86.

jam’,⁵⁹² where two different opinions are declared jointly valid for applications in different times or conditions. Although this tool is merely of a scholastic nature and has no bearing on enforcement, it can be used to harmonise various opinions and minimise differences before setting a standard. Another possible tool suggested by Baker is the use of *talfiq*,⁵⁹³ amalgamation or “the fusing of different legal opinions”,⁵⁹⁴ where a jurist combines different views to establish an opinion that is not accepted as a whole by any one school.⁵⁹⁵ For instance, to justify a Shari‘ah-compliant product, a scholar might rely on a structure which has one component recognised by the Ḥanafī school and another other part recognised by another school. Yet no school of the thought will validate the whole structure. However, while such a tool has been used to draft a code for Islamic law,⁵⁹⁶ the extensive use of *talfiq* might widen existing disagreements and can lead to circumventing the substance of the Shari‘ah by selecting a combination of views which serve the interest of a single individual or institution.⁵⁹⁷

In addition, institutionalising the process of product approval as well as promoting the issuing of collective *fatwas* would limit the inconsistency in *fatwas*.⁵⁹⁸ Such a governing institution should be aware of how Shari‘ah-compliant products are applied in practise and take into consideration the objective of Islamic finance. It is generally

⁵⁹² Kamali, *Principles of Islamic Jurisprudence*, p228; al-Turkī, *Asbāb Akhtil-āaf al-Fuqahā*’, p267.

⁵⁹³ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance."

⁵⁹⁴ Birgit Krawietz, "Cut and Paste in Legal Rules: Designing Islamic Norms with Talfiq," *Die Welt des Islams* 42, no. 1 (2002): p3.

⁵⁹⁵ See: Nāṣir al-Maymān, "al-Talfiq fi al-Ijtihād wa al-Taqlīd," *Majalh al-‘adl* 3, no. 11 (2001): p4; Muḥammad Sa‘īd al-Bānī, *‘Umdah al-Taḥqīq fi al-taqlīd wa al-talfiq*, ed. Ḥasan Suāyḍān, 2nd ed. (Dār al-Qādirī, 1998), p183.

⁵⁹⁶ Coulson, *A History of Islamic Law*, p197.

⁵⁹⁷ See generally: al-Bānī, *‘Umdah al-Taḥqīq fi al-taqlīd wa al-talfiq*, p224.

⁵⁹⁸ Osāmah al-Ashqar, *Fawḍā al-Ifṭā* (Dār al-Nfā’is, 2009), p99.

accepted that juristic opinions which are in line with the objective of Shari‘ah should prevail over the ones that only comply with the letter of the law.⁵⁹⁹

However, as may be apparent, the aforementioned tools are more of a scholastic nature and are not directly related to standardisation. The central issue is not which opinion is the right interpretation, but rather how to enforce it, and indeed whether enforcing a particular opinion can be justified in Shari‘ah. Historically, attempts to tackle the issue have used political will to standardise different rulings. One of the earliest examples cited in the literature is a suggestion made by ‘AbdAllāh Ibn al-Maḡaffa‘ (d.139/757).⁶⁰⁰ Unsatisfied with the inconsistent rulings of jurists, he wrote a memorandum addressed to the Abbasid caliph at that time, Abū Ja‘far al-Manṣūr (d. 159/775), urging him to use his political power to end the conflict in jurists’ *fatwas*. He argued that Islamic law is divided into two parts, “the non-derogable or uninteruptable and the variable or interpretable”.⁶⁰¹ The former includes absolute obligations which are not open to discretion. For example, the ruler has no choice but to implement prayers and fasting. The latter is the non-definitive part of the Shari‘ah, which is open to interpretation, and the ruler has the authority to enforce the most appropriate opinion for the public interest. In response, the caliph al-Manṣūr asked Mālik Ibn Anas, the founder of Mālikī school of thought in Medina, to author a book which would be enforced across the empire. Mālik later received a similar suggestion from another caliph, Hārūn al-Rashīd (d.193/808). However, although Mālik authored the book, he advised the caliphs not to enforce it. He argued that some of the juristic

⁵⁹⁹ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p87.

⁶⁰⁰ See: Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p292.; Joseph E. Lowry, "The First Islamic Legal Theory: Ibn al-Muḡaffa' on Interpretation, Authority, and the Structure of the Law," *Journal of the American Oriental Society* 128, no. 1 (2008): p153; Yḡyā al-Khilālyh, "Taḡnīn al-Sharī‘ah al-Islāmiyyh bayn al-Nazzrīh wa al-Taṭbīq" (PhD thesis International Islamic University, 2002).

⁶⁰¹ Lowry, "The First Islamic Legal Theory: Ibn al-Muḡaffa' on Interpretation, Authority, and the Structure of the Law," p30.

views in Medina might not be accepted by the people of Iraq, who might have adopted a different set of legal theories based on *ḥadīth* reported by the Prophet's companions who moved to Iraq after his death.⁶⁰² The debate at that time was very strong between the school of *ahl al-raʿy*⁶⁰³ in Iraq and *ahl al-ḥadīth*⁶⁰⁴ (the traditionalists) in Medina. Islamic jurisprudence was in its formative period, and the major four schools of thought had not yet been formed as schools of distinct principles.⁶⁰⁵ As an alternative solution,⁶⁰⁶ the caliph al-Rashīd appointed Abū Yūsuf, an authoritative Ḥanafī scholar, as a Chief Justice. Abū Yūsuf was responsible for appointing judges in the empire who were mostly said to be followers of the Ḥanafī school.⁶⁰⁷

Nevertheless, classical Shariʿah jurists seem to have realised the scope of the problem and have formed two legal maxims to tackle the issue of conflicting opinions. The first one states that a ruling of a judge shall conclude the disagreement between scholars on that particular issue (*ḥukm al-ḥākim yarfaʿ al-khilāf*).⁶⁰⁸ For example, if jurists have conflicting views over the validity of a certain contract, and a judge has favoured one view, then that view is the enforceable one in that judge's jurisdiction. On a larger scale, if a state has selected the view of one school of thought on a specific legal matter, it is the only valid view in that jurisdiction. A party might

⁶⁰² Masud, "Ikhtilaf al-Fuqaha: Diversity in "Fiqh" as a Social Construction" p66.

⁶⁰³ *Ahl al-raʿy* school (literally: the people of good sense) generally includes those in favour of using independent legal argumentations as a method of concluding a Shariʿah ruling. See: Hennigan, "Ahl al-raʿy."

⁶⁰⁴ *Ahl al-ḥadīth* school includes those who endeavour to base the law on the Prophetic Traditions and the Prophet's Companions. According to their view, it is illegitimate to favour or solely rely on unrestricted human reasoning, especially when it conflicts with an authentic *ḥadīth*. See Joseph Schacht, "Ahl al-Ḥadīth," *ibid.* <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/ahl-al-hadith-SIM_0379>

⁶⁰⁵ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p292.

⁶⁰⁶ Riḍwān al-Sayyid, "al-Fiqh wa al-Siyāsah fī al-Tajrubah al-Islāmiyyah al-Wasīṭah," *Majalah al-Tafāhum*, no. 25 (2009).

⁶⁰⁷ Ismāʿīl al-Aghbarī, "Taqnīn al-Fiqh al-Islāmī: Qānūn al-Aḥwāl al-Shakhṣiyyah al-ʿUmānī Unmūdḥajan," Taddart, http://www.taddart.org/ar/?p=12767#_ftn18. accessed 8 October 2012.

⁶⁰⁸ Muḥammad Ṣḍqī al-Būrṅū, *Mawsūʿah al-Qawāʿid alFfghyyh*, vol. 5 (Maktabah al-Tawbah, 2000), p72.

not be able to reject the enforcement of a judge's ruling on the ground that it conflicts with the opinions of other Shari'ah scholars. Al-Jaṣṣāṣ (d.370/981),⁶⁰⁹ an authoritative Ḥanafī scholar, states that "all scholars agree that when a judge relies on one jurisprudential view in his judgment, his decision shall be enforceable and shall not be rejected on the ground of other *ijtihād*. It shall be enforceable even if the two parties believe otherwise". Similarly, al-Qarāfī (d.684/1285),⁶¹⁰ a renowned Mālikī scholar, upholds the statement of al-Jaṣṣāṣ and goes further to state that according to the view of the majority of scholars, jurists belonging to other schools of thought should change their *fatwas* to correspond to the judicial decision.

The second legal maxim which completes the first one is that an *ijtihād* of a judge cannot be revoked by an *ijtihād* of other judges in the future (*al-ijtihād lāa yunqaḍ bimithlih*).⁶¹¹ For example, if a disputed contract was validated by a judge from the Ḥanafī School, it cannot be invalidated by another judge who belongs to another school of thought. Also, if the same judge changes his view in the future, it cannot be applied retrospectively to his old cases. Both legal maxims were justified in the classical books by their ability to ensure stability in transactions and prevent conflicts.⁶¹²

Although such legal maxims might have worked in the Caliphate state, they are not sufficient to work in today's model of the state. Therefore, many contemporary jurists have strongly advocated the idea of codifying Islamic jurisprudence to solve

⁶⁰⁹ Aḥmad 'alī al-Jaṣṣāṣ, *Aḥkām al-Qur'ān*, ed. Muḥamad al-Ṣādiq Qamḥāwī, vol. 1 (Dār Iḥyā' al-Turāth al-'arabī, 1985), p316.

⁶¹⁰ Aḥmad Idrīs al-Qarāfī, *al-furūq*, ed. Khalīl al-Manṣūr, vol. 2 (Dār al-Kutub al-'ilmiyyh, 1998), p179.

⁶¹¹ Muḥammad Ṣdqī al-Būrñū, *Mawsū'ah al-Qawā'id alFqhyyih*, vol. 1 (Maktabah al-Tawbah, 2000), p430.

⁶¹² See: al-Qarāfī, *al-furūq*, 2, p180.

the issue of inconsistency.⁶¹³ For example, Muṣṭafā al-Zarqā (d.1420/1999),⁶¹⁴ a renowned Shari‘ah scholar, emphasises the need to enforce a code which is not restricted to one school of thought. He acknowledges that diversity of opinions in Islamic jurisprudence can offer a window of ease for Muslims in different times and circumstances. However, while he regards unifying *fatwas* as almost impossible,⁶¹⁵ he believes that codifying a particular view in the form of written rules is a necessity in today’s world to establish legal certainty.⁶¹⁶ This is because a *fatwa* issued by a Shari‘ah scholar is not binding, while *ḥukum* (judgement) which is issued by a Shari‘ah scholar who at the same time is appointed by the authority as a judge is binding. Both are religious opinions, but the latter has an enforcing power.⁶¹⁷

Any attempts to unify *fatwas* will be difficult to enforce even if there is political will. In 2010, the Saudi king issued a royal decree restricting the issuing of public *fatwas* to the members of the official Council of Senior Ulemas and to those licensed by the Council.⁶¹⁸ However, in the age of the Internet and social media, such a rule is hardly followed. In fact, it might encourage people to seek a *fatwa* from more independent scholars.⁶¹⁹ Hence, a degree of uncertainty in terms of conflicting *fatwas* will always exist.

⁶¹³ For an extensive debate about the codifying of Shari‘ah, see: Abdulmomen Shuja'a Aldeen, "Mawqif al-Fuqahā' min Taqnīn Aḥkām al-Sharī'ah al-Islāmiyah," *Organization House of Law* <http://ohlyemen.org/modules.php?name=News&file=article&sid=110> accessed 10 June 2012; al-Khilālyh, "Taqnīn al-Sharī'ah al-Islāmiyyh bayn al-Nazzrīh wa al-Taṭbīq."; Muḥamaad Zakī ‘Abdālbar, *Taqnīn al-Fiqh al-Islāmī*, ed. ‘AbdAllāh al-Anṣārī (Dār al-Turāth al-Islāmy, 1986); ‘Abd al-Raḥman al-Jar‘ī, "Taqnīn al-Fiqh al-Islāmī Bayn al-Māni‘īn Wa al-Mujīzīn," *Islam Today*(2005) <http://islamtoday.net/bohooth/artshow-86-5987.htm> accessed 15 July 2012.

⁶¹⁴ Muṣṭafā al-Zarqā, *al-Madkhal al-Fiqhī al-‘ām*, vol. 1 (Dār al-Qalam, 1998), p314.

⁶¹⁵ *Fatwas* issued by Shari‘ah scholars are not binding, while *ḥukum* (judgment) is issued by a Shari‘ah scholar who is appointed by the authority as a judge. Both are religious or legal opinions, but the latter has an enforcing or binding power.

⁶¹⁶ Muṣṭafā al-Zarqā, *al-Fiqh al-Islāmī Wa Madārisah* (Dār al-Qalam, 1995), p86.

⁶¹⁷ al-Ashqar, *Fawdā al-Iftā*, p13.

⁶¹⁸ Al Arabiya News, "Saudi king limits clerics allowed to issue fatwas," Alarabiya.net, <http://www.alarabiya.net/articles/2010/08/12/116450.html>. accessed 8 September

⁶¹⁹ See for example: Christopher Boucek, "Saudi Fatwa Restrictions and the State-Clerical Relationship," Carnegie Endowment for International Peace,

Nevertheless, judicially enforcing one opinion should maintain certainty and eventually limit the effect of other *fatwas* in the industry. One of the earliest examples of codifying Islamic jurisprudence was the *Majallah al-Aḥkām al-‘Adliyah* set of civil laws for Muslims written during the Ottoman Caliphate (1876 CE).⁶²⁰ It consists of 1,851 articles based on the jurisprudence of the Ḥanafī school of thought.⁶²¹ Following this, several attempts were made to codify Islamic jurisprudence according to major schools of thought by the Islamic Research Academy of Al-Azhar University, the Arab League, and individual scholars.⁶²² However, a better measure would be for a proactive regulatory body to assume the responsibility of enforcing *ijtihād* in the Islamic finance industry, as is the case in countries such as Malaysia, Pakistan, and Sudan, which have established a central Shari‘ah supervisory board.⁶²³

It is important to note that selecting one interpretation as the national standard does not mean that other views are wrong or are non-Islamic.⁶²⁴ Rather, it means this particular view will be enforced by authorities in that particular state for the sake of stabilising the financial market and establishing certainty in the judicial system. Also, it does not mean that the standards adopted by the authority cannot be changed in the future. As with any modern rules or standards, Shari‘ah standards can be changed and updated to accommodate new needs or circumstances.

However, standardising Shari‘ah interpretation through a governmental body has two main limitations. First, it might not be possible in secular countries where

<http://www.carnegieendowment.org/sada/?fa=aboutSada>. accessed 12 September 2012; al-Ashqar, *Fawḍā al-Iftā*, p72.

⁶²⁰ Turkey, *The Mejelle: Being an English Translation of Majallah El-Ahkam-i-Adliya and a Complete Code on Islamic Civil Law*, trans. Charles Robert Tyser, D. G. Demtriades, and Ismail Haqqi Effendi (Islamic Book Trust, 2001).

⁶²¹ Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," 293.

⁶²² Ibid.; Aldeen, "Mawqif al-Fuqahā' min Taqnīn Aḥkām al-Sharī'ah al-Islāmiyah". p8; al-Khilālyh, "Taqnīn al-Sharī'ah al-Islāmiyyh bayn al-Nazzrīh wa al-Taṭbīq," p154.

⁶²³ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁶²⁴ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p88.

authorities lack the legal power or the will to enforce such standards. For example, the former Financial Services Authority in the UK⁶²⁵ was aware of the importance of standardisation, yet they have clearly stated that they do not have the legal standing to intervene in a religious matter, although generally encouraging the effort of Shari‘ah standard-setting organisations such as AAOIFI and the IFSB.⁶²⁶ Nevertheless, the general duties of regulators to protect consumers and maintain financial stability can provide justification for a regulatory body to instruct an IIFS to be more transparent with its clients and to disclose which school of thought its product complies with, rather than using the general label of “Shari‘ah compliant”.

Secondly, since there is no accepted international Shari‘ah standard, enforcing a particular Shari‘ah interpretation might be problematic for an IIFS active in multiple jurisdictions,⁶²⁷ as some of its products can be regarded as Shari‘ah compliant in one country and not Shari‘ah compliant in another. Khan and Feddad⁶²⁸ have suggested a gradual global standardisation of Shari‘ah ruling in Islamic finance. However, establishing a global Shari‘ah standard might be ineffective due to the lack of political will in different countries, and compliance with such a standard cannot be enforced or supervised unless it is enforced by national regulators.⁶²⁹ It has been mentioned earlier that although the AAOIFI standard was intended to be an international standard, and

⁶²⁵ As of 2013, the responsibilities of the FSA have been divided among two new separate entities, the Financial Conduct Authority and the Prudential Regulation Authority. See: United Kingdom, "Financial Services Act 2012".

⁶²⁶ Michael Ainley et al., *Islamic Finance in The UK : Regulation and Challenges* (London: Financial Services Authority,, 2007), p16; Antonio, "What is the Future Outlook of Shar'iah Harmonization?," p14.

⁶²⁷ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁶²⁸ Habib Ahmed, "Islamic Law, Adaptability and Financial Development " *Islamic Economic Studies* 13, no. 2 (2006): p93. Since AAOIFI also sets accounting standards for Islamic financial institutions, they suggest the establishing a new nonprofit organisation (International Organization of Standards for Shari‘ah Application in Finance Industry) which solely focuses on this task.

⁶²⁹ Oxford Analytica, "Islamic Finance Moves Toward Common Standards" p4; Ghoul, "The Standardization Debate in Islamic Finance: A Case Study ".

is approved by Shari‘ah scholars from different schools of thought and sects, it is in practise enforced by very few countries at the national level.

To overcome these limitations, effort should be directed towards establishing a global Shari‘ah standard which classifies different practises of Islamic finance even if they are deemed controversial or highly disputed.⁶³⁰ The standard should not state the prevalence of any jurisprudential view, but rather it should list the requirements for implementing each particular view. IIFS can use it as a reference to disclose to regulators, consumers, and rating agencies which *fatwa* or school of thought they are adopting.⁶³¹ This should allow for a better assessment of the compliance level of the institution. Given the difficulty associated with establishing such standards, Khan⁶³² suggests setting an international body similar to International Organization for Standardisation (ISO), which could be called the “International Organization for Standardisation for Shari‘ah Application in the Finance Industry (IOSSAFI)”. Although Khan does not clarify who would oversee this body and how it would be funded, the broad nature of the suggested standard which accommodates various schools of thought can overcome the limitations of existing standards such as the one issued by AAOIFI. It can be used by any financial institution around the world irrespective of whether it is operating in an Islamic or secular country. With an appropriate mechanism of disclosure, it is hoped that the market would eventually adopt best practises and avoid controversial ones such as the contract of *‘inah*.⁶³³

⁶³⁰ See: Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p304; Abdulbari Mashal, "al-Raqābah al-Shar‘iyyah llimashrif al-Markazī ‘alā al-Mu’sasāt al-Māliyyh al-Islāmiyyh" (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15/5/2005), p21.

⁶³¹ See Khan, "Setting Standards for Shariah Application in The Islamic Financial Industry," p293.

⁶³² Ibid., p303.

⁶³³ Laldin notes that the market already has started to shift from the controversial practise of Islamic finance to a less controversial one. See: Remo-Listana, "Islamic Finance Standardisation Needs to be Tackled Carefully".

4.6. Conclusion

This chapter has aimed to examine the suitability of standardisation as a mechanism to reduce conflict in the opinions of Shari‘ah scholars concerning the permissibility of financial products. This inconsistency in the *fatwas* issued by SSBs is a key factor contributing to the issue of creative Shari‘ah compliance. The study showed that juristic differences are inevitable and pose a serious challenge to compliance in the Islamic finance industry. After addressing the causes of the disagreements between Shari‘ah scholars, it argued that it is possible for a state to enforce a particular Shari‘ah interpretation and that such a solution has been justified by classical and contemporary Shari‘ah jurists. However, it might be difficult to use this remedy at a global level due to the lack of political will or legal power to regulate religious matters in secular countries. Accordingly, this chapter has suggested that efforts be directed towards establishing a Shari‘ah standard which codifies various practises of Islamic finance, even if they are deemed highly controversial. Such well-defined standards would facilitate the task of regulators, courts, and rating agencies, as well as gradually encouraging IIFS to be more transparent with their clients about which fatwa or school of thought they are adopting, rather than using the general label of “Shari‘ah compliant”. With such a level of disclosure, the market would hopefully move towards adopting best practises.

The next chapter examines how Shari‘ah supervisory board governance practises contribute to the issue of creative Shari‘ah compliance in contemporary Islamic finance.

Chapter Five:

The Impact of Shari‘ah Governance Practises on Shari‘ah Compliance in Contemporary Islamic Finance

5.1. Introduction

This chapter examines the extent to which Shari‘ah supervisory board (SSB) governance practises contribute to the issue of creative Shari‘ah compliance in the contemporary Islamic finance industry.⁶³⁴ To gain the trust of their Muslim clients, institutions offering Islamic financial services (IIFS) normally incorporate a religious board in the form of an SSB. In theory, the SSB is there to ensure that IIFS operate within Shari‘ah norms and teachings. However, concerns have been raised about the feasibility of a viable and functional Shari‘ah governance culture in IIFS. Doubts relate mainly to these boards’ unclear functions and legal status, lack of accountability and transparency, and conflicts of interest and lack of independence, as well as to the poor training and inadequate qualifications of SSB members.

This chapter argues that the prevalence of these critical governance issues largely reduces the level of Shari‘ah compliance in the Islamic finance industry. Thus, the chapter recommends that regulators in Islamic and secular countries intervene and regulate Shari‘ah governance in IIFS so as to ensure a sound financial system and investor confidence. The chapter is structured in five parts including this introduction. Part 5.2 explores definitions of SSBs in Islamic finance literature; Part 5.3 highlights the importance of SSBs in IIFS structure; Part 5.4 examines the impact of regulatory issues surrounding SSBs on Shari‘ah compliance in the contemporary Islamic finance

⁶³⁴ An early version of chapter five was published under the following citation: Alkhamees, Ahmad. “The Impact of Shari‘ah Governance Practises on Shari‘ah Compliance in Contemporary Islamic Finance.” *Journal of Banking Regulation* 14, no. 2 (10 September 2012): 134–63.

industry, identifying seven challenges as major factors in reducing the level of Shari‘ah compliance in IIFS; and finally, Part 5.5 concludes the chapter.

5.2. Shari‘ah Supervisory Board Definition

The literature does not provide a standard definition or name for SSBs or for Shari‘ah supervision more generally.⁶³⁵ SSBs have variously been called, for example, Shari‘ah committees, religious committees, Shari‘ah councils, and *fatwa* authorities.⁶³⁶ However, “SSBs” seems to be the more common term in recent literature and is preferred by international standard-setting bodies such as the Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).⁶³⁷

Definitions found in the literature fall into two broad categories.⁶³⁸ The first one includes definitions that focus on the functional aspect of SSBs and the objectives they seek to achieve. In this category, the IFSB’s “Guiding Principles on the Shari‘ah Governance System” uses the term “Shari‘ah Governance System”, which refers to a “set of institutional and organisational arrangements through which an IIFS ensures that there is effective independent oversight of Shari‘ah compliance”.⁶³⁹ Similarly, the older standard-setting body, the AAOIFI, defines

⁶³⁵ Samy Nathan Garas and Chris Pierce, "Shari'a Supervision of Islamic Financial Institutions," *Journal of Financial Regulation and Compliance* 18, no. 4 (2010): p387.

⁶³⁶ Zighībah "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Ḥulūl Muqtarahah " p13.

⁶³⁷ See: Islamic Financial Services Board (IFSB), "Guiding Principles on Shariah Governance Systems for Institutions Offering Islamic Financial Services," IFSB,, <http://www.ifsb.org/standard/IFSB-10%20Shariah%20Governance.pdf>. accessed 29 March 2011; Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Accounting, Auditing & Governance Standards for Islamic Financial Institutions " in *Shari'a Review* (Bahrain: AAOIFI, 2002).

⁶³⁸ Riyād Muḥammad al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay'āt al-Shar'iyyah " (paper presented at the Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 5-6/10/2003), p16.

⁶³⁹ Islamic Financial Services Board (IFSB), "IFSB Guiding principles on Shariah governance systems for institutions offering Islamic financial services".

Shari‘ah supervision as the process of examining the institution’s commitment to adherence to Shari‘ah in all its activities.⁶⁴⁰

Abū Ghuddah provides a more detailed definition in this first category.⁶⁴¹ According to him, Shari‘ah supervision is a process of examination and analysis of activities, actions, and processes undertaken by the institution to certify that they are in accordance with the provisions and principles of Islamic law. SSBs should use appropriate means to identify errors and suggest legitimate solutions to correct them, in addition to submitting a report which incorporates Shari‘ah opinions and decisions along with recommendations for earning lawful income in the present and the future.⁶⁴²

The second category includes definitions stressing the nature of the body entrusted with the task of Shari‘ah supervision. In this regard, al-Şāliḥ defines SSBs as a group of jurisprudence scholars and economists who direct and supervise bank activities to ensure compliance with the provisions of Shari‘ah.⁶⁴³ al-Shabīlī’s definition emphasises the legal status of SSB resolutions. He defines SSBs as bodies comprising a number of scholars who specialise in *fiqh al-mu‘āmalāt* (Islamic commercial jurisprudence), issue binding Shari‘ah guidelines, and supervise their enforcement to ensure correct implementation.⁶⁴⁴

⁶⁴⁰ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Accounting, Auditing & Governance Standards for Islamic Financial Institutions".

⁶⁴¹ ‘Abd al-sattār Abū Ghuddah, "al-Usus al-Fanniyyah lil-rraqābah al-Shar‘iyyah Wa ‘Alāqatuhā Biālttadqīq al-Shar‘ī Fī al-Mu‘asasāt al-Māliyyah al-Islāmiyyah " *hawliyyah al-Barakah* 4, no. November (2002): p6.

⁶⁴² Ibid.

⁶⁴³ Muḥammad Aḥmad al-Şāliḥ, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maşārif al-Islāmiyyah " (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009), p6.

⁶⁴⁴ Yūsuf ‘AbdAllāh al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maşārif:Ḍawābiṭhā Wa Aḥkāmhā Wa Dawrhā fī Ḍabṭ ‘Amal al-Maşārif" (ibid.), p2.

The disparities in SSB names and definitions are a vestige of different stages of development in modern Islamic finance.⁶⁴⁵ They also reveal the confusion over the role and function of SSBs, which may vary from one institution to another according to the legal environment in which they operate, an issue that Part 4.4 of this chapter discusses in detail.

5.3. The Importance of SSBs

Compliance with Shari‘ah is one of the fundamental values of Islam. Muslims are required to adhere to the principles of Islam in every aspect of their lives, including their financial transactions.⁶⁴⁶ The importance of SSBs results from the fact that only scholars who are well versed in Shari‘ah have the competence to judge whether or not certain products or services are consistent with Islamic law. In the early stages of Islamic history, traders were accompanied by a scholar who advised them on lawful transactions. In the present climate, IIFS executives do not have sufficient knowledge or time to acquire the relevant expertise to evaluate Islamic finance. Therefore, the presence of SSBs in the IIFS structure is crucial to assist IIFS directors in conducting Shari‘ah-compliant services and businesses.⁶⁴⁷

Another feature which highlights the importance of SSBs in IIFS structure is that as a group of respected scholars, board members provide stakeholders with crucial confidence and assurance that IIFS management does not violate Shari‘ah in its business.⁶⁴⁸ Public confidence is a vital element of any financial institution profile. In

⁶⁴⁵ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p16.

⁶⁴⁶ Ayub, *Understanding Islamic Finance*, p475.

⁶⁴⁷ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p388.; al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p5.

⁶⁴⁸ Hussain Gulzar Rammal, "The Importance Of Shari‘ah Supervision In Islamic Financial Institutions," *Corporate Ownership and Control Journal* 3, no. 3 (2006).

a survey conducted by Hassan et al.,⁶⁴⁹ respondents unanimously agreed that SSBs play a significant role in this regard. In short, IIFS cannot market businesses as Shari'ah compliant without the presence of an SSB, which provides institutions with an Islamic identity.⁶⁵⁰

Furthermore, SSBs add economic value to Islamic financial institutions. Their performance increases institutional profits by innovating Shari'ah-compliant products and services.⁶⁵¹ Moreover, SSBs can play an indirect role in marketing IIFS businesses when they take part in different conferences and workshops around the world.⁶⁵² By contributing to the media and giving public lectures, they utilise their knowledge and social position to inform people about Islamic finance and to convince stakeholders to support Shari'ah-compliant products.

Having an SSB also reduces the legal costs of IIFS and minimises exposure to Shari'ah risk.⁶⁵³ The involvement of an SSB in the early development of a product can save IIFS from having to pay legal expenses at a later date to bring the product in line with Islamic law.⁶⁵⁴ It also mitigates the risk of engaging in non-Shari'ah-compliant activities, which may be deemed beyond the capacity of the institution and call into question the enforceability of existing contracts in Muslim and secular countries.⁶⁵⁵

⁶⁴⁹Rusni Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* (Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance ISRA 2010), p11&44.

⁶⁵⁰ Aldohni, "Islamic Banking Challenges Modern Corporate Governance: The Dilemma of The Shari'a Supervisory Board."; Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* p44.

⁶⁵¹ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p388; al-Khalīfī, "al-Nazariyyah al-Āmmah Lil-hay'āt al-Shar'iyyah" p8-11.

⁶⁵² El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p11.

⁶⁵³ Shari'ah risk "is the possibility that a financial service or product is not or will not be in compliance with established Shari'ah principles and standards." See: Yusuf Talal DeLorenzo, "Shari'ah Compliance Risk," *Chicago Journal of International Law* 7, no. 2 (2007). The enforceability of a contract in Muslim and secular countries might be called into question, as one of the parties might lack the capacity to sign a non-Shari'ah-compliant contract. Djojosingito, "Mitigating Legal Risk in Islamic Banking Operations."

⁶⁵⁴ Yusuf Talal DeLorenzo, "Shari'ah Supervision in Modern Islamic Finance," <http://www.nzibo.com/IB2/Shari'ahsupervision.pdf>. accessed 8 February 2011

⁶⁵⁵ For more about Shari'ah risk, see: "Shari'ah Compliance Risk." 'Shari'ah Compliance Risk'

In addition to reducing legal costs, SSBs can be a legal requirement of providing Islamic financial services. In countries such as Malaysia,⁶⁵⁶ Jordan,⁶⁵⁷ Kuwait,⁶⁵⁸ and Lebanon,⁶⁵⁹ regulators require the presence of an SSB in the institution as a condition for offering any Shari'ah-compliant services.⁶⁶⁰ An SSB may also be required for admission to certain international institutions, as in the case of the International Association of Islamic Banks (IAIB).⁶⁶¹

However, the need for SSBs has been questioned from two different perspectives. First, Mudawi⁶⁶² argues that Islamic financial institutions which operate within a country where Islamic law is applied may not need to have an SSB, as the state should have its own mechanism to issue any required *fatwas* and resolutions. This argument seems to be based on a misunderstanding of the role of SSBs. Ensuring IIFS compliance with Shari'ah is not just about issuing *fatwas* or reviewing products a single time; rather, it is a continuing process of monitoring which starts when the product is being structured and ends when the product is implemented. In addition, this argument assumes that IIFS operate locally in a model Islamic state, where the state plays a major role in the religious affairs of the public. It ignores the fact that such a body does not exist in many Muslim countries, where states follow a secular system. Even where such official organs exist, they are unlikely to have sufficient resources and expertise to deal with complex financial instruments. It is also doubtful

⁶⁵⁶ "(ACT 701) Central Bank of Malaysia Act " Bank Negara Malaysia,, http://www.bnm.gov.my/documents/act/cba2009_01.pdf. accessed 4 April 2011

⁶⁵⁷ "Law No. 28 of 2000," Jordan central bank http://www.cbj.gov.jo/pages.php?menu_id=123&local_type=0&local_id=0&local_details=0&local_details1=0&localsite_branchname=CBJ. accessed 11 September 2011, article 58

⁶⁵⁸ "CBK Law No. (32) of 1968," CBK http://www.cbk.gov.kw/www/law_iii.html#ch3_10. accessed 8 September 2011 article 93

⁶⁵⁹ "Law No 575 dated February 11, 2004 The Establishment of Islamic Banks in Lebanon," Banque du Liban http://www.bdl.gov.lb/circ/lawpdf/Law575_en.pdf. accessed 24 September 2011 article 9

⁶⁶⁰ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p389.

⁶⁶¹ Ibrahim Warde, *Islamic Finance in The Global Economy* (Edinburgh: Edinburgh University Press, 2000), p226.

⁶⁶² Al Bagkir Yousif Mudawi, "Organization in Islamic Banking," *Journal of IB&F* 1[2], no. 2 (1984). Cited in: Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* p14.

that such entities could be efficient enough to meet the demands of a business environment.

The second challenge to the need for an SSB argues that the presence of an SSB is a formality,⁶⁶³ since IIFS management can easily access the most recent research and training courses provided by institutions—for instance, the Institute of Islamic Banking and Insurance or the IIUM Institute of Islamic Banking and Finance.⁶⁶⁴ This argument shares the first question's unclear understanding of SSB function. It overlooks the complexity of Islamic finance, even for those trained in Shari'ah in general. It also discounts stakeholders' lack of confidence in IIFS executives' compliance with Shari'ah. In short, the need for SSBs in IIFS is similar to the need for lawyers in the conventional finance industry: even given its long-term establishment and rich resources, the industry still needs legal advisors to structure its financial products.

With the importance and the definitions of SSB addressed, the following section examines the extent to which SSB governance practises contribute to the issue of creative Shari'ah compliance in the contemporary Islamic finance industry.

5.4. Regulatory Issues Surrounding Shari'ah Supervisory Boards

5.4.1. *The Ambiguous Role of SSBs*

As discussed, the main purpose for establishing SSBs in financial institutions is to oversee the Shari'ah compliance of IIFS business activities.⁶⁶⁵ However, there is no standard in the industry to clearly define how SSBs should perform this task. The scope of SSB work varies from one institution to another, and there is no agreement

⁶⁶³ Warde, *Islamic Finance in The Global Economy*, p228; Rammal, "The Importance Of Shari'ah Supervision In Islamic Financial Institutions," p204-05.

⁶⁶⁴ Warde, *Islamic Finance in The Global Economy*, p228; Rammal, "The Importance Of Shari'ah Supervision In Islamic Financial Institutions," p204-05.

⁶⁶⁵ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p388.; al-Khalīfī, "al-Nazariyyah al-`Āmmah Lil-hay'āt al-Shar'īyyah " p5.

on the duties of its members.⁶⁶⁶ In fact, many institutions sign contracts with Shari‘ah supervisors without specifying the nature of the work, their rights, or their duties.⁶⁶⁷ Accordingly, while some SSBs have a proactive role in institutions, which might involve operational tasks, others might not even hold a single meeting or issue one decision during a whole year.⁶⁶⁸ The ill-defined description of SSB roles and duties could be regarded as a bad governance practise which might contribute to weak compliance in the industry.

The vague scope of SSB function is arguably traceable, in part, to different phases of historical development in modern Islamic finance. In the early days of Islamic finance, around 1970, IIFS mainly used Shari‘ah scholars as a marketing tool to promote the ideology of Islamic finance in their societies.⁶⁶⁹ The process of issuing a *fatwa* to approve the permissibility of products was less formal and conducted in a non-institutional style.⁶⁷⁰ A member of the public or a company would provide a Shari‘ah scholar with a brief description of the products or the contract, and then the scholar would issue a *fatwa* either approving or rejecting it. In fact, until 2000, most SSB scholars at Al Rajhi Bank, one of largest Islamic banks in Saudi Arabia,

⁶⁶⁶ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". p17; Muḥammad ‘Abd al-Ḥalīm ‘Umar, "A‘māl al-Hay‘āt al-Shar‘iyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu‘assasiyyah " (paper presented at the The Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 7-8/10/2003), p17.

⁶⁶⁷ Muḥammad Amīn ‘Alī Qaṭṭān, "Hay‘ah al-Raqābah al-Shar‘iyyah Akhtiyār A‘dā’ihā Wa Ḍawābiṭhā " (paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, Bahrain, 27-28/5/2008), p11.

⁶⁶⁸ Ahmad Muḥammad al-Sa‘ad, "al-Raqābah al-Shar‘iyyah Wa’ Atharhā Fī al-Maṣārif al-Islāmiyyah" (paper presented at the The Third International Conference on Islamic Economics, Mecca, 31/5-2/06/2005), p28.

⁶⁶⁹ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p76-78; ‘Umar, "A‘māl al-Hay‘āt al-Shar‘iyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu‘assasiyyah " p12.

⁶⁷⁰ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay‘āt al-Shar‘iyyah " p5.

reviewed the Shari'ah compliance of its products and contracts on a volunteer basis and sent their decision to the external auditor of the bank.⁶⁷¹

The existence of various institutions offering different levels of Islamic financial service might also have contributed to uncertainty about the SSB role. While some IIFS were fully established as Islamic banks, others gradually converted their services at a later stage to those of Islamic banks, or only offer Islamic windows as an additional service to their main conventional banking.⁶⁷²

Furthermore, few regulators around the globe have recognised Shari'ah supervision as an independent profession overseen by a regulatory body.⁶⁷³ Even where it is officially acknowledged as a profession, as in Pakistan and Bahrain, SSB members might not have a legal status that requires performing specific tasks related to their speciality.⁶⁷⁴

Like the industry, academic research also seems to be confused over SSBs. A variety of classifications, duties, and assumptions appears in Islamic finance literature discussing the functions of SSB members.⁶⁷⁵ Al-Khalīfī, for example,⁶⁷⁶ classifies the

⁶⁷¹ Muḥammad Anas Muṣṭafā al-Zarqā, "al-Haykal al-Shar'ī Lil-ṣṣinā'at al-Māliyyah al-Islāmiyyah Jawānib al-Khalal wa Ṭarīq al-İslāh " (paper presented at the Symposium on Values and Morals For The Work of Economic Institutions, Kuwait 30/3/2008), p3. It is worth noting that during this time, SSBs were not responsible for *ex post* Shari'ah review.

⁶⁷² For a general view of the experience of converting conventional banks to Islamic banks: Ibrāhīm Muṣṭafā Muṣṭafā, "Taḳyīm Zāhirah Taḥawul al-Bunūk al-Taqlīdiyyah Lil-maṣrifīyyat al-Islāmiyyah Dirāsah Taḳbīḳiyyah 'an Tajribah Ba'ḍ al-Bunūk al-Su'ūdiyyah " (Master thesis, American Open University 2006).

⁶⁷³ See: 'Umar, "A' māl al-Hay'āt al-Shar'iyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " p17; Abdalaziz Ibn Sṭtam al-Saud, "Siyāsah al-Jawdah al-Shar'iyyah fī al-Maṣrifīyaah al-Islāmiyyah," *al-Fiqh al-Islāmī*(2011) <http://www.islamfeqh.com/News/NewsItem.aspx?NewsItemID=4004> accessed 10 May 2012

⁶⁷⁴ Malaysia is an exception with regard to recent BNM updates, see: Bank Negara Malaysia (BNM), "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)," Bank Negara Malaysia, http://www.bnm.gov.my/guidelines/05_shariah/02_Shariah_Governance_Framework_20101026.pdf. accessed 11 December 2010; Omar Mustafa Ansari, "Roles and responsibilities of shariah advisors in Islamic banking institutions", *True Banking* <http://www.alhudacibe.com/AlhudaMagazine/Issue-036/article05.php>. accessed 10 May 2013

⁶⁷⁵ See for example: al-Ṣāliḥ, "Dawr al-Raqābah al-Shar'iyyah Fī Ḍabṭ a' māl al-Maṣārīf al-Islāmiyyah " p6; Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p393-95; Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* ; Muḥammad Amīn 'Alī Qaṭṭān, "al-Raqābah al-Shar'iyyah al-Fa'ālah Fī

scope of SSB functions into four areas: reviewing contracts and financial transactions and agreements, reviewing general policies of the financial institution, reviewing internal codes and regulations, and monitoring the conduct of financial institution staff in terms of its code of ethics. The first area is the centre of most SSB work in the industry. The effort of its members is mainly concentrated on fulfilling this role, and a couple of advanced steps have been made in this regard. This is partly because contracts and financial products represent the main activities of IIFS, so they naturally allocate the most effort to this area.

The general policies of the second area include reviewing the financial institution's investment policies, for example, recommending a focus on equity-based rather than debt-based products, as the former are more desirable from an Islamic finance development perspective. It also includes monitoring accounting policies, for instance, ensuring the fairness of profit and loss allocation in Islamic investment accounts, assets evaluation, and *zakāh* calculation. Finally, this area involves supervising marketing policies to ensure that they do not breach the principles of Shari'ah. For instance, giving commissions and gratuities to some company staff to win a contract is deemed a type of bribery, which is prohibited under Islamic law.

The third area of responsibility that Al-Khalīfī describes includes ensuring the Shari'ah compliance of internal codes and rules, which regulate the running of the institution and the duties and rights of its employees, shareholders, and stakeholders. Al-Khalīfī cites the example of an Islamic bank in Kuwait, where the articles of association clearly state that any overdue payment of capital is subject to a substantial 7% annual interest rate. Such a clause directly violates the prohibition of usury in

al-Maṣārif al-Islāmiyyah " (paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/06/2005), p29-33; Qaṭṭān, "Hay'ah al-Raqābah al-Shar'iyyah Akhtiyār A'ḍā'ihā Wa Ḍawābiḥā " p17.

⁶⁷⁶ al-Khalīfī, "al-Naẓariyyah al-Āmmah Lil-hay'āt al-Shar'iyyah " p44-53.

Shari‘ah. The fourth area involves the inspection of the code of conduct of IIFS staff to ensure that it meets the ethical standards of Shari‘ah, which include, *inter alia*, honesty and fairness in contracts and transactions, commitment to promises and appointments, the effective implementation of agreements, and avoidance of fraud, corruption, and all disgraceful deeds or behaviour.⁶⁷⁷

These areas of responsibility show how wide the scope of SSBs actually is, and how unlikely individual boards are to fully oversee all these areas in practise, particularly in secular countries. Nevertheless, a typical list of SSB duties in an Islamic financial institution can include the following⁶⁷⁸:

1. Issuing *fatwas* to approve IIFS financial instrument products.
2. Auditing the process of applying SSB decisions through the Shari‘ah internal review unit.
3. Certifying that IIFS have conducted their business according to Shari‘ah by issuing an annual shareholder report.
4. Calculating the required *zakāh* and advising management on channelling non-Shari‘ah compliant revenue towards charitable activities.
5. Approving the distribution of loss and profit between investment account holders and shareholders.
6. Educating and training IIFS staff on Shari‘ah principles, responding to clients’ inquiries, and increasing social awareness of Islamic finance objectives.
7. Developing new Shari‘ah-compliant products and services.

⁶⁷⁷ Ibid.

⁶⁷⁸ See: Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services"; Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p77; al-Şāliḥ, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maşārif al-Islāmiyyah " p6; Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p12-18; Warde, *Islamic Finance in The Global Economy*, p363-87; Zighībāh "Hay’āt al-Fatwā Wa al-Riqābah al-Shar‘iyyah Fī al-Mu‘asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu‘awwiqāt ‘Amalhā wa Ḥulūl Muqtaraḥah " p25; Garas and Pierce, "Shari‘a Supervision of Islamic Financial Institutions," p393-94.

Although these responsibilities are often mentioned in the literature, few SSBs perform all these tasks in practise. In fact, most SSBs are only concerned with *ex ante* Shari‘ah review without auditing how products are actually implemented in the market.⁶⁷⁹ Besides, some SSB members are still debating whether some of these duties, such as developing products, should be included amongst their responsibilities.⁶⁸⁰

This overload of duties suggests that SSB functions have been shaped without an appreciation of the current framework of global financial markets, which legally requires IIFS to assign certain tasks to “Approved Persons”.⁶⁸¹ It seems that the ambitious goal of ensuring Shari‘ah compliance has even led some SSB members to overlook the political systems of most countries. This assumption can be supported by the following three examples.

First, it was suggested that SSBs can play a vital role in controlling financial offences in IIFS, because financial crimes, such as fraud, manipulation, and insider dealing, are prohibited under the rule of Shari‘ah. Therefore, ensuring Shari‘ah compliance should theoretically prevent such illegal activities from occurring. However, it is unlikely that SSB members would have the necessary expertise and resources or the legal authorisation to undertake such a task.⁶⁸²

Secondly, as a solution to weak Shari‘ah compliance at a micro level, it has been suggested that the Shari‘ah compliance officer should be appointed as a branch

⁶⁷⁹ al-Sa‘ad, "al-Raqābah al-Shar‘iyyah Wa’ Atharhā Fī al-Maṣārif al-Islāmiyyah," p19; Rammal, "The Importance Of Shari‘ah Supervision In Islamic Financial Institutions."; ‘AbdAllāh Furayḥ al-Bahlāl, "al-Raqābah al-Shar‘iyyah Fī al-Bunūk al-Su‘ūdiyyah " (Master thesis Imam University, Higher Institute of Justice, 2003), P141.

⁶⁸⁰ Garas and Pierce, "Shari‘a Supervision of Islamic Financial Institutions," p394; Abdulbari Mashal, "al-‘Affāq al-Mustaqbaliyyah Lil-rriqābah al-Shar‘iyyah Ru‘yah Lil-ttaṭwīr " (paper presented at the About The Future of Islamic Finance: Exploring The Opportunities of Tomorrow, Kuala Lumpur, 25-27/10/2010), p11.

⁶⁸¹ See for example: Financial Conduct Authority (FCA), "What is an approved person?," FCA, <http://www.fca.org.uk/firms/being-regulated/approved/approved-persons>. accessed 4 April 2014

⁶⁸² Siti Faridah Abd Jabbar, "Financial crimes: Prohibition in Islam and prevention by the Shar‘a Supervisory Board of Islamic financial institutions," *Journal of Financial Crime* 17, no. 3 (2010).

manager.⁶⁸³ Similarly, the Malaysian Central Bank recommends the appointment of an SSB chairman as a non-executive director on the IIFS board.⁶⁸⁴ The Faisal Islamic Bank in Cyprus did so, arguing that it would enable the SSB to communicate effectively with the board of directors and that it would be in a better position to ensure the Shari‘ah compliance of the institution.⁶⁸⁵ On the other hand, it is doubtful whether such an action would be tolerated in countries such as the UK, where a “Fit and Proper Test for Approved Persons” is required before an individual can register under the Financial Conduct Authority’s Approved Persons regulations.⁶⁸⁶ In addition, there is the question of whether most SSB scholars with multiple memberships would successfully pass the non-executive director independence test.⁶⁸⁷

In some institutions such as the Al Rajhi Bank, SSB duties involve the additional human resources function of selecting the institution’s employees, particularly for key positions. Candidates for employment are assumed to support Islamic finance policies and to be willing to implement their practise.⁶⁸⁸ Although having personnel with a proper understanding of Islamic finance principles enhances Shari‘ah compliance in an institution, such a task can be achieved without the involvement of SSB members, as this might possibly threaten their disinterested auditing.

⁶⁸³ ‘Ādil ‘AbdAllāh Bāryān, "Asālib Tafīl Dawr al-Raqābah al-Shar‘iyyah Fī al-Maṣārif al-Islāmiyyah" (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5-3/6/2009), p27.

⁶⁸⁴ Habhajan Singh, "BNM mulls 5 Shariah Advisors for Islamic Banks", *Malaysian Reserve* 25 October 2010 <http://islamicfinanceasia.blogspot.com/2010/10/bnm-mulls-5-shariah-advisors-islamic.html>. accessed 10 December 2010

⁶⁸⁵ Qaṭṭān, "al-Raqābah al-Shar‘iyyah al-Fa‘ālah Fī al-Maṣārif al-Islāmiyyah" p21.

⁶⁸⁶ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*, p13-14., also: Financial Services Authority, "Approved persons," FSA,, <http://www.fsa.gov.uk/Pages/Doing/Regulated/Approved/persons/index.shtml>. accessed 24 December 2011

⁶⁸⁷ On non-executive directors’ independence, see: Christine A. Mallin, *Corporate Governance* (Oxford; New York: Oxford University Press, 2010), p174-75.

⁶⁸⁸ Alrajhi Bank, "The Sharia Group," <http://www.alrajhibank.com.jo/AboutUs/Pages/ShariaaGroup.aspx>. accessed 10 December 2010

Finally, it has been suggested that SSBs should play a mediating role between IIFS and their clients.⁶⁸⁹ For instance, Article 18 of Act 48 on the establishment of Faisal Islamic Bank of Egypt states that in the case of the parties' refusal to choose an arbitrator, or in the absence of an agreement on the choice of chairmen in an arbitral tribunal, the SSB will choose an arbitrator or chairman, and its decision will be binding. However, the Supreme Constitutional Court of Egypt ruled this article unconstitutional, as it breaches the principles of arbitration and denies a natural right of access to court.⁶⁹⁰

As can be seen from the diverse functions mentioned earlier, ambiguity clearly surrounds the actual duties of SSB members. The ensuring of Shari'ah compliance, which is the main purpose of establishing an SSB, has been weakened as its members are engaged in unrelated tasks which they might not be qualified to perform. To overcome such confusion, Shari'ah supervision should first be recognised as an independent profession.⁶⁹¹ Like lawyers and accountants, its members should act within a framework that defines their role and responsibilities. In the case where an IIFS is operating within a jurisdiction which does not facilitate Islamic finance compliance or where regulation is passive, SSB members can form a professional association that standardises its supervisors' contracts with financial institutions. Alternatively, it is possible to state SSB functions in an institution's articles of association.⁶⁹² In addition, SSB functions ought to be categorised according to the level of Shari'ah-compliant activities that their home institution conducts. The SSBs

⁶⁸⁹ Qaṭṭān, "Hay'ah al-Raqābah al-Shar'iyyah Akhtiyār A'ḍā'ihā Wa Ḍawābiḥā " p17; Qaṭṭān, "al-Raqābah al-Shar'iyyah al-Fa'ālah Fī al-Maṣārif al-Islāmiyyah " p33.

⁶⁹⁰ *The Supreme Constitutional Court of Egypt, Case No. 13 of year 15 6408(1994).*

⁶⁹¹ 'Umar, "A'māl al-Hay'āt al-Shar'iyyah Bayn al-Istishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " p17.

⁶⁹² See generally, Rafel Mahmood, "Islamic Governance, Capital Structure, and Equity Finance: Examining the Possibilities of American Financial Shari'ah Boards," *International Journal of Legal Information* 37, no. 1 (2009). Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p389.

in Islamic banks, for example, tend to have a greater role than their counterparts in conventional banks which only offer Islamic windows. Stakeholders should be made aware of this discrepancy, which might affect the institution's degree of compliance.

5.4.2. SSBs' Lack of Legal Status

A related but separate issue affecting the Shari'ah compliance of IIFS is the SSBs' lack of legal status. In some countries, there is no legal basis for establishing an SSB in Islamic finance institutions. Even where there are legal provisions, it is not clear whether SSB decisions are deemed mandatory or merely advisory. This section investigates the legal position of SSBs and its impact on the Shari'ah compliance of institutions.

An SSB can draw its legal authority from different sources. In countries such as Malaysia,⁶⁹³ Pakistan,⁶⁹⁴ UAE,⁶⁹⁵ Kuwait,⁶⁹⁶ Jordan,⁶⁹⁷ and Lebanon,⁶⁹⁸ national regulations require establishing an SSB before granting Islamic financial services. In addition, IIFS articles of association might include provisions for setting up an SSB and defining its power.⁶⁹⁹ A lower ground of SSB authority can be based on the terms of the contract signed between the board of directors, on behalf of shareholders, and the SSB, where rights are awarded to review IIFS business.

⁶⁹³ Bank Negara Malaysia (BNM), "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)".

⁶⁹⁴ State Bank of Pakistan, "Instructions for Shariah Compliance In Islamic Banking Institutions," State Bank of Pakistan <http://www.sbp.org.pk/ibd/2008/Annex-c2-1.pdf>, accessed 25 January .Section A

⁶⁹⁵ "Federal Law No-(6) of 1985 concerning Islamic Banks and Financial Institutions and Investment Companies," Central Bank of United Arab Emirates <http://www.centralbank.ae/pdf/LawNo6-1985-IslaminBanks.pdf>, accessed 10 November 2011, Article 6

⁶⁹⁶ "CBK Law No. (32) of 1968", Article 93

⁶⁹⁷ "Law No. 28 of 2000", Article 58

⁶⁹⁸ "Law No 575 dated February 11, 2004 The Establishment of Islamic Banks in Lebanon", Article 9

⁶⁹⁹ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p389.

However, some Shari‘ah scholars offer a different perspective for legitimatising SSB power.⁷⁰⁰ According to them, the authority of the SSB stems from the Islamic notion of *hisbah*, where individual Muslims have a duty to command right behaviour and forbid wrongdoing to keep society in line with the teachings of Islam. Accordingly, SSB members have a natural duty to ensure that IIFS activities are conducted within Shari‘ah.⁷⁰¹ However, the nature of SSB work does not suit the concept of *hisbah*. This is because SSB members are appointed and paid privately to ensure the Shari‘ah compliance of the institution, whereas *muhtasib* (a person conducting *hisbah*) is more concerned with public matters and is usually appointed and paid by the state.⁷⁰² Besides, in modern states, *hisbah* in Islamic countries is restricted to moral issues and antisocial behaviour.⁷⁰³

Even where legal grounds are found for establishing an SSB, though, it is not clear whether SSB judgments have an advisory nature or a mandatory one.⁷⁰⁴ If they are merely advisory, then the primary motivation for setting up SSBs—that is, ensuring Shari‘ah compliance—has not been achieved. The role of SSBs is narrowed to that of a marketing tool, as the boards’ decisions are only enforced at the IIFS administration’s pleasure. Countering this situation, the AAOIFI Shari‘ah governance standard states that SSB pronouncements shall be binding and fully implemented.⁷⁰⁵

⁷⁰⁰ ‘AbdAllāh Mabruk al-Najjār, "Muftariḍāt al-Mas’ūliyyah fī Niṭāq al-Raqābah al-Shar‘iyyah ‘alā al-Mu’assasāt al-Māliyyah " (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UEA, 26/4/2009), p13-14.

⁷⁰¹ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p14; Zighībāh "Hay’āt al-Fatwā Wa al-Riqābah al-Shar‘iyyah Fī al-Mu’assasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu‘awwiqāt ‘Amalhā wa Ḥulūl Muqtaraḥah " p37.

⁷⁰² al-Najjār, "Muftariḍāt al-Mas’ūliyyah fī Niṭāq al-Raqābah al-Shar‘iyyah ‘alā al-Mu’assasāt al-Māliyyah " p13-27.

⁷⁰³ For more about *hisbah* see: M. A. Cook, *Commanding Right and Forbidding Wrong in Islamic Thought* (Cambridge, UK; New York: Cambridge University Press, 2000).

⁷⁰⁴ Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p54.

⁷⁰⁵ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), " No. 1 - Shari‘a Supervisory Board: Appointment, Composition and Report.," in *AAOIFI Governance Standard for Islamic Financial Institutions* (Bahrain: AAOIFI, 1999) Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p81.

Nevertheless, even where such a standard is adopted, or where regulators or IIFS articles of association have stipulated the mandatory nature of SSB decisions, these measures are insufficient to ensure compliance with Shari‘ah, because SSBs only issue *fatwas* on cases brought to them by IIFS management.⁷⁰⁶ In other words, if directors think the SSB will not approve a particular transaction, they can avoid the issue simply by not referring the matter to the Shari‘ah board. This helps explain why some regulators and academic researchers have suggested appointing one of the SSB members as a non-executive director on the board of the financial institution.⁷⁰⁷ However, it is unlikely that Shari‘ah scholars, with their multiple memberships in SSBs in different institutions, would successfully fulfil the independence requirements for a position as either an executive or non-executive director.⁷⁰⁸

In addition, designating SSB decisions as mandatory may raise concerns amongst regulators over their impact on the financial institution’s operations.⁷⁰⁹ Although researchers such as Aldohni⁷¹⁰ have argued that forming a Shari‘ah board in a UK corporate structure is not legally problematic, since the Companies Act 2006 is elastic with regard to a two-tier board structure,⁷¹¹ they overlook the legal issues arising from the Financial Conduct Authority (FCA) requirements for persons to be appointed on such a board. The “Fit and Proper Test for Approved Persons”, mentioned above,

⁷⁰⁶ ‘Umar, "A‘māl al-Hay‘āt al-Shar‘iyyah Bayn al-I‘lāshihāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu‘assasiyyah " p11; ‘Abd al-Razzāq Raḥīm al-Hītī, "Athar al-Raqābah al-Shar‘iyyah ‘alā Ail-tizām al-Maṣārif al-Islāmiyyah bi-al-’Aḥkām al-Shar‘iyyah " (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5/2009 - 3/6/2009), p19; ‘Abd al-Mun‘im Muḥammad al-Ṭayyib, "Taḥqīm al-Raqābah al-Shar‘iyyah fī Zīl al-Niẓām al-Maṣrifi al-Islāmī al-Shāmil" (ibid.31/5- 3/6/2009), p26.

⁷⁰⁷ Singh, "BNM mulls 5 Shariah Advisors for Islamic Banks."

⁷⁰⁸ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*, p13-14.

⁷⁰⁹ Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p79; ‘Aṭiyyah Fayyād, "al-Raqābah al-Shar‘iyyah Wa al-Taḥaddiyāt al-Mu‘āshirah " (paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/6/2005), p40.

⁷¹⁰ Aldohni, "Islamic Banking Challenges Modern Corporate Governance:The Dilemma of The Shari‘a Supervisory Board," p157; Paul L. Davies, *Introduction to Company Law* (Oxford: Oxford University Press, 2010), p195.

⁷¹¹ Aldohni, "Islamic Banking Challenges Modern Corporate Governance:The Dilemma of The Shari‘a Supervisory Board," p157; Davies, *Introduction to Company Law*, p195.

considers competence and capability factors, among other things.⁷¹² It expects that a person appointed for a directorial position has sufficient relevant experience, a condition which might not be met by most SSB members, who tend to lack financial and banking experience.

Rider⁷¹³ notes that SSB members in most common law countries can be regarded as shadow directors⁷¹⁴ if the board of directors regularly acts on SSB advice. This designation means that SSB members are subject to same legal duties as directors, and in some situations, they can be held accountable for misconduct and negligence in the general management of the company. Rider continues, however, that issuing SSB advice in a professional capacity is not alone sufficient to deem SSB members shadow directors. Additional factors are taken into account to determine whether a person is a shadow director; for example, he must be in a dominant position and not appointed to a particular post within the structure of the company.⁷¹⁵ Notably, although Jamieson and Hughes⁷¹⁶ note that English law remains unsettled on the identification of shadow directors, SSB members might meet the criterion of being in a dominant position in situations where the management of a fully flagged Islamic bank needs *ex ante* or *ex post* approval of SSB members to engage in business contracts.

⁷¹² See: Financial Conduct Authority (FCA), "What is an approved person?"; "The Fit and Proper test for Approved Persons," FCA, <http://media.fshandbook.info/content/FCA/FIT.pdf>. accessed 4 April 2014

⁷¹³ Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," p168.

⁷¹⁴ A shadow director is defined as "a person in accordance with whose directions or instructions the directors of the company are accustomed to act (but so that a person is not deemed a shadow director by reason only that the directors act on advice given by him in a professional capacity)". See: United Kingdom, "Company Directors Disqualification Act 1986," The National Archives, http://www.legislation.gov.uk/ukpga/1986/46/pdfs/ukpga_19860046_en.pdf. accessed 10 May 2013 Chapter 46 Section 22.

⁷¹⁵ Rider notes that recent court decisions show a more flexible position over what constitutes a shadow director. See: Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," p168.

⁷¹⁶ Neil Jamieson and Kelly Hughes, "The Identification of Shadow Directors under English law: what guidance might Buzzle provide?," *Butterworths Journal of International Banking and Financial law*. 27, no. 6 (2012): p366.

Currently, the FCA considers the SSB's role merely advisory.⁷¹⁷ This characterisation can seriously reduce the level of Shari'ah compliance in institutions, since IIFS management has no compulsion to enforce SSB decisions regarding compliance in its products and services. For an SSB to ensure Shari'ah compliance, it must be involved in decisions that affect the operational aspect of the financial institution.⁷¹⁸ The AAOIFI standard states that Shari'ah supervisors are "entrusted with the duty of directing, reviewing and supervising the activities related to Islamic finance to ensure they are in compliance with Shari'ah rules and principles. The views of the Shari'ah advisor shall be binding in the specific area of supervision".⁷¹⁹ In short, an SSB cannot ensure true Shari'ah compliance unless its decision is deemed mandatory and is enforced in practise.

Accordingly, in terms of the real function of SSBs, a legal status needs to be considered for SSB members, who currently hold a unique position somewhere between being external auditors and non-executive directors.⁷²⁰ Indeed, recognising Shari'ah supervision as an independent profession would help to shape the legal standing of SSB members. Nevertheless, the weight of Shari'ah board pronouncements against IIFS management's decisions and the consequences of

⁷¹⁷ See: Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p110.

⁷¹⁸ Ezry Fahmy, "Shari'ah Scholars as an Independent Director: A Proposal", *Shirkah* <http://www.scribd.com/doc/50058751/3/Comprehend-the-position-of-Independent-director-and-Shari%E2%80%99ah-Scholars>. accessed 10 May 2011

⁷¹⁹ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), " No. 1 - Shari'a Supervisory Board: Appointment, Composition and Report."

⁷²⁰ Interestingly, while English literature in the area seems to indicate the resemblance of SSB members' roles to those of non-executive directors, most Arabic literature highlights the similarity of SSBs to external auditors. Compare Aldohni, "Islamic Banking Challenges Modern Corporate Governance: The Dilemma of The Shari'a Supervisory Board."; Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*; Fahmy, "Shari'ah Scholars as an Independent Director: A Proposal," p16; Rodney Wilson, "Regulatory Challenges Posed by Islamic Capital Market Products and Services," *Journal of Islamic Banking and Finance* 24[2], no. 2 (2007); Hussain Hamed Hassan, "al-'Alāqah Bayn al-Hay'āt al-Shar'iyyah wa al-murāji'īn al-khārijīyyīn " (paper presented at the The First Conference for Shari'a Supervisory Boards, Bahrain, 9/10/2001); al-Zarqā, "al-Haykal al-Shar'i Lil-ṣṣinā'at al-Māliyyah al-Islāmiyyah Jawānib al-Khalal wa Ṭarīq al-Iṣlāḥ "; Mohamad Akram Laldin, "Dawr al-Raqābah al-Shar'iyyah Fī Ḍabṭ a'māl al-Maṣārif al-Islāmiyyah" (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UEA, 26/4/2009).

breaching SSB pronouncements need to be addressed by regulators,⁷²¹ or at least be stated in the IIFS articles of association. Currently, some of IIFS personnel do not comply with SSB decisions unless those decisions are authorised by the directors of the financial institution.⁷²² In other words, an IIFS charter should include a default clause which identifies the relationship between the board of directors and the SSB, as well as the applicable procedure for addressing a conflict between the two boards.

Moreover, conflict between the two bodies can be further reduced if a financial institution's articles of association characterise it as an entity that fully complies with Shari'ah ruling.⁷²³ In Saudi Arabia, where there is no framework for Shari'ah governance in the financial sector,⁷²⁴ Al Rajhi Bank has clarified its policy towards the power of the SSB: it regards SSB decisions as obligatory for the departments and management of the institution. Executive directors on all levels are responsible for implementing SSB resolutions. Any violation of SSB pronouncement while offering products or services, without seeking prior authorisation from the board, is firmly prohibited, and all culpable are disciplined.⁷²⁵ Such steps seem to be more visible than involvement from regulators, particularly in non-Islamic countries.

⁷²¹ For example, Article 17 from the Yemeni act on Islamic banks states that SSB decisions on the compliance of bank instruments are to be binding on the institution. The SSB shall issue an annual report on the bank's adherence to Shari'ah and to SSB instructions, and this report must be distributed to shareholders. Yemen, "Act 21(1996) as amended by Act 16 (2009) on Islamic Banks in Yemen," Central Bank of Yemen, http://www.centralbank.gov.ye/App_upload/Islamic_Pank_low_Ar_Upd.pdf, accessed 8 July 2011

⁷²² al-Ṭayyib, "Taḳyīm al-Raqābah al-Shar'īyyah fī Zīl al-Nizām al-Maṣrifī al-Islāmī al-Shāmil," p28. al-Sa'ad, "al-Raqābah al-Shar'īyyah Wa' Atharhā Fī al-Maṣārif al-Islāmiyyah," p17.

⁷²³ Mahmood, "Islamic Governance, Capital Structure, and Equity Finance: Examining the Possibilities of American Financial Shari'ah Boards."

⁷²⁴ Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p97.

⁷²⁵ Alrajhi Bank, "The Sharia Group".

5.4.3. SSBs' Lack of Accountability

Accountability in a general sense has deep roots in Islam,⁷²⁶ as all individuals are accountable to God for their actions. People's destiny in the hereafter is determined according to their deeds in this world. The word *ḥisāb* (account) is mentioned at least eight times in the Quran,⁷²⁷ which states that on the Day of Judgment, Allah will show each person his account, where all good and bad actions are recorded.⁷²⁸ In theory, Muslims cannot separate their life into religious and secular aspects, since all their economic, political, religious, and social activities are bound up with the teachings of Shari'ah.⁷²⁹

However, one of the factors affecting compliance in the Islamic finance industry is the lack of accountability for SSB members. Surprisingly, such an essential body in the institution, with great power over the direction of the market, is exempt from scrutiny and liability.⁷³⁰ Islamic finance regulations and standards, such as those of the AAOIFI, completely disregard this issue. Even in countries with an advanced Shari'ah governance framework, such as Malaysia and Pakistan, SSB accountability is poorly addressed.⁷³¹ Their frameworks do mention procedures for dismissing SSB members, but not in the context of accountability.⁷³²

⁷²⁶ Mervyn K Lewis, "Accountability and Islam," *Fourth International Conference on Accounting and Finance*(2006) <http://www.unisa.edu.au/commerce/docs/Accountability%20and%20Islam.pdf> accessed 25 July 2011

⁷²⁷ Ibid.

⁷²⁸ The Quran, in verses 54:52-53, states that "All that they do is noted in [their] Books [of Deeds]: Every matter small and great is on record". Similarly, verses 99:7-8 have, "Then shall anyone who has done an atom's weight of good, see it! And anyone who has done an atom's weight of evil, shall see it". Abdullah Yusuf Ali, *The Holy Qur'an :Text, Translation and Commentary* (Brentwood, Md.: Amana Corp, 1983).

⁷²⁹ Zafar Iqbal and Mervyn Lewis, *An Islamic Perspective on Governance* (Cheltenham, U.K.; Northampton, Mass.: Edward Elgar, 2009), p257.

⁷³⁰ Wright, "The Shariah Scholar Cartel"; Aldohni, "Islamic Banking Challenges Modern Corporate Governance:The Dilemma of The Shari'a Supervisory Board," p159.

⁷³¹ As stand on 31 August 2011.

⁷³² Muḥammad 'Abd al-Ghaffār al-Sharīf, "al-Raqābah al-Shar'iyyah 'Alā al-Mu'assasāt al-Tamwīliyyah al-Islāmiyyah" (paper presented at the TheThird International Conference on Islamic Economics, Mecca, Mecca, 31/5-2/6/2005), p16-17; al-'Yāashiy al-Şādiq Fidād, "al-Raqābah al-Shar'iyyah Wa Dawruhā Fī Dabṭ A'māl al-Maşārif al-Islāmiyyah" (paper presented at the 19th session

Arguably, SSB liability is overlooked for two main reasons, the first of which is the lack of legal status amongst SSBs. As discussed earlier, in most countries, Shari‘ah board members have no legal standing in financial institutions, making it difficult to hold them liable for actions over which they have no legal power. Even where SSBs are officially recognised, there is no legislation detailing their liability and incriminating their wrongdoing.⁷³³ The second reason which might prove an obstacle to SSB accountability is that SSB members are usually highly respected in society; they are perceived as guardians of Shari‘ah who fear no one but Allah.⁷³⁴ Although there is no infallibility for Shari‘ah scholars in Islam,⁷³⁵ some ordinary Muslims seem to see criticism of Shari‘ah scholars as criticism directed towards Islam itself.⁷³⁶

Nonetheless, historically, scholars have debated whether a *mujtahd* (a person who practises *ijtihād*) is liable for *ijtihād*.⁷³⁷ The majority position is that the *mujtahd* is not liable for any mistakes in his *fatwas* since he issues rulings to the best of his ability.⁷³⁸ The grounds for this position is the *ḥadīth* of the Prophet which states that when the

of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009), p21. However, unlike Pakistan, the BNM Shari‘ah Governance Framework for Islamic Financial Institutions at least alludes to the accountability of SSB members. See: Bank Negara Malaysia (BNM), "Shari‘ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p11.

⁷³³ Sulaymān Na‘īm al-Rā‘ī, "Athar Hay‘āt al-Fatwā wa al-Riqābah al-Shar‘iyyah Fī al-Mu‘asasāt al-Māliyyah al-Islāmiyyah " (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005), p370; Bāryān, "Asālib Taf‘īl Dawr al-Raqābah al-Shar‘iyyah Fī al-Maṣārif al-Islāmiyyah " p24.

⁷³⁴ For a general description of the role of the Shari‘ah scholar, see: Joseph A Kechichian, "The Role of the Ulama in the Politics of an Islamic State: The Case of Saudi Arabia," *International Journal of Middle East Studies* 18, no. 1 (1986): p55.; Meir Hatina, *Guardians of Faith in Modern Times : `Ulama in The Middle East* (Boston: Brill, 2009).

⁷³⁵ Charles P. Trumbull, "Islamic Arbitration: A New Path for Interpreting Islamic Legal Contracts," *Vanderbilt Law Review* 59, no. 2 (2006): p627.

⁷³⁶ Aly Khorshid, "Shariah Board Accountability," Academy UK, <http://www.academyuk.org/publications/view.aspx?id=19>. accessed 10 December 2010

⁷³⁷ According to Wael B. Hallaq, *ijtihād* "is the maximum effort expended by the jurist to master and apply the principles and rules of *usuul al-fiqh* (legal theory) for the purpose of discovering God's law." Hallaq, "Was the Gate of Ijtihad Closed?."

⁷³⁸ al-Najjār, "Muftariqāt al-Mas‘ūliyyah fī Niṭāq al-Raqābah al-Shar‘iyyah ‘alā al-Mu‘asasāt al-Māliyyah " p38-39; ‘Abd al-Sattār al-Khuwaylidī, "al-Ākhtiṣāṣ al-Qānūnī Wa al-Ḥimāyah al-Jinā‘iyyah Lil-hay‘āt al-Shar‘iyyah " (paper presented at the Third Conference of Shari‘a Supervisory Boards of Islamic Financial Institutions, Bahrain, 5-6/10/2003), p8-9; Fidād, "al-Raqābah al-Shar‘iyyah Wa Dawruhā Fī Ḍabṭ A‘māl al-Maṣārif al-Islāmiyyah," p22.

ruler performs *ijtihād* and reaches the right conclusion, he will be rewarded twice, but if he makes an error, he will be rewarded just once for making the *ijtihād*.⁷³⁹ The only exceptions to this position occur when a definitive principle has been breached or when an individual has issued a *fatwa* without having the competence to do so.⁷⁴⁰

However, this section is not primarily concerned with the classical discussion of scholarly liability in this context, but rather with the harm that arises from an SSB's failure to fulfil its duties—for example, declaring a financial institution Shari'ah compliant without carrying out a sufficient review, deliberately failing to report violations of Shari'ah in a product or service, not holding SSB meetings, or allowing frequent absences in meetings. Such negligence might cause a great deal of damage to stakeholders and increase the risk profile of institutions, which is unlawful in Shari'ah teaching.⁷⁴¹

Indeed, increasing SSB accountability should enhance the quality of Shari'ah compliance in the institution. This is because Shari'ah board members would ideally scrutinise IIFS activities closely to avoid risking any legal responsibility. Currently, SSBs are not liable for any damage arising from their remissness; they lose nothing from circumventing Islamic finance restrictions.⁷⁴² The worst-case scenario for its members is termination of their contract, which is unlikely as it might cause further

⁷³⁹ Rushdi Siddiqui, "A Sharia Scholar's Place on The Board," Gulf News, <http://gulfnews.com/business/features/a-sharia-scholar-s-place-on-the-board-1.625445>. accessed 30 October 2010

⁷⁴⁰ 'Abd āl-Ḥamid al-Ba'ī, "al-Raqābah al-Shar'iyyah al-Fa'ālah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah " (paper presented at the TheThird International Conference on Islamic Economics, Umm Al Qura University, Mecca, 31/5-02/06/2005), p39. Some jurists have stated that in case, the scholar was incompetent, IIFS may take the responsibility for not conducting due diligence. See al-Najjār, "Muftariḍāt al-Mas'ūliyyah fī Niṭāq al-Raqābah al-Shar'iyyah 'alā al-Mu'assasāt al-Māliyyah " p38-39.

⁷⁴¹ Qaṭṭān, "al-Raqābah al-Shar'iyyah al-Fa'ālah Fī al-Maṣārif al-Islāmiyyah " p23-25.

⁷⁴² Lahem al-Nasser, "Waḍ' al-Maṣrifīyyah al-Islāmiyyah Murbik Wa Naḥn Biḥājah ilā Wilādah Jadīdah ", *Islamic Finance and Investment* 01/09/2010 http://www.almasrifiah.com/2010/09/01/article_438969.html. accessed 1 November 2010

damage to the institution. In *Investment Dar v Blom Development Bank*,⁷⁴³ the claimant argued in its legal defence that the contract in question was not Shari'ah-compliant, despite the fact that it had been approved by its own Shari'ah board. The SSB of Investment Dar did not announce its resignation or sue the company to protest the challenge to its credibility. It merely issued a majority statement backing up its old ruling and asking the company not to use SSB decisions in further litigation.⁷⁴⁴ If SSBs were held accountable for such incidents, we would have seen a stronger reaction.

An additional accountability issue requiring clarification is whether the responsibility for ensuring Shari'ah compliance lies with the SSB or with the management of the IIFS. While some researchers suggest that ensuring Shari'ah compliance is the responsibility of the SSB,⁷⁴⁵ others suggest that it is the responsibility of IIFS executive directors, and that SSB responsibility ends with forming Shari'ah opinion on the compliance of proposals for products or services without concern for their actual implementation.⁷⁴⁶ The AAOIFI standard seems to support the latter stance.⁷⁴⁷ Such a position is understandable if one assumes that the AAOIFI considers the SSB's role as merely an advisory one, with no impact on the operational aspect. However, as discussed earlier, AAOIFI standards also state that

⁷⁴³ *Investment Dar Co KSCC v Blom Developments Bank Sal.*

⁷⁴⁴ Shaheen Pasha, "Investment Dar gets Sharia Board blow to Blom Case," Arabian Business, <http://www.arabianbusiness.com/investment-dar-gets-sharia-board-blow-blom-case-282707.html>, accessed 14 July 2011; al-Nasser, "Waḍ' al-Maṣrifiyyah al-Islāmiyyah Murbik Wa Naḥn Biḥājah ilā Wilādah Jadīdah".

⁷⁴⁵ For example, al-Shabīlī, "al-Raqābah al-Shar'iyyah 'Alā al-Maṣārif: Dawābiḥā Wa Aḥkāmḥā Wa Dawrhā fī Ḍabṭ 'Amal al-Maṣārif," p22; Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p76.

⁷⁴⁶ 'Abd al-Ḥaq Ḥamīsh, "Hay'ah al-Fatwā Wa al-Raqābah al-Shar'iyyah Fī al-Maṣārif al-Islāmiyyah" (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15/5/2005), p339; Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

⁷⁴⁷ Ahmad Muḥī al-dīn Ahmad, "Ḥudūd al-Hay'āt al-Shar'iyyah Wa Idārāt al-Mu'assasāt al-Māliyyah al-Islāmiyyah Fī al-Ta'akud min al-Āltizām Biāl'Aḥkām al-Shar'iyyah" (paper presented at the Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 5-6/10/2003), p17. Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "No. 1 - Shari'a Supervisory Board: Appointment, Composition and Report.."

Shari‘ah supervisors are “entrusted with the duty of directing, reviewing and supervising the activities related to Islamic finance to ensure they are in compliance with Shari‘ah rules and principles. The views of the Shari‘ah adviser shall be binding in the specific area of supervision”.⁷⁴⁸ Consequently, it is not safe to leave SSB members holding such power without sharing responsibility for their actions. Nonetheless, Al-Khalīfī and other researchers argue that ensuring Shari‘ah compliance is not only a duty of the SSB, but also the collective responsibility of stakeholders.⁷⁴⁹

Finally, when discussing SSB members’ accountability, it is often argued that Shari‘ah scholars are held accountable to God.⁷⁵⁰ These ‘*ulamā*’ or scholars are assumed to be the most trusted people, who would never compromise or hide the truth. The Quran states, “It is only those who have knowledge among His slaves that fear Allah”.⁷⁵¹ Iqbal and Lewis⁷⁵² note that Islam regards some governance problems, such as corruption, as ethical issues which can be resolved by enhancing internal strength rather than by applying external legal forces. In contrast, the majority of Western scholars seem to deem corruption to be the result of bad governance, rather than focusing on its moral dimension. The authors suggest that Islamic countries can

⁷⁴⁸ " No. 1 - Shari’a Supervisory Board: Appointment, Composition and Report.."

⁷⁴⁹ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p21; al-Hīfī, "Athar al-Raqābah al-Shar‘iyyah ‘alā Ail-tizām al-Mašārif al-Islāmiyyah bi-al-’Aḥkāmī al-Shar‘iyyah " p14; ‘Ādil ‘AbdAllāh Bāryān, "Asālīb Tafīl Dawr al-Raqābah al-Shar‘iyyah Fī al-Mašārif al-Islāmiyyah " (ibid.31/5- 3/6/2009), p47.

⁷⁵⁰ Aldohni, "Islamic Banking Challenges Modern Corporate Governance:The Dilemma of The Shari’a Supervisory Board," p158; Wright, "The Shariah Scholar Cartel".

⁷⁵¹ Taqī al-Din Hilali and Muhammad Muhsin Khan, "The Noble Quran," Muslim Directory, <http://quran.com/35/28>. accessed 7 August 2011. Ibn Katheer commented on this verse: “Only those who have knowledge truly fear Him as He should be feared, because the more they know about the Almighty, All-Powerful, All-Knowing Who has the most perfect attributes and is described with the most beautiful Names, the more they will fear Him.” Ismail ibn Umar Ibn Kathir, "Tafsir Ibn Kathir " Darussalam, http://www.qtafsir.com/index.php?option=com_content&task=view&id=1906&Itemid=. accessed 8 August 2011

⁷⁵² Iqbal and Lewis, *An Islamic Perspective on Governance*, p306-12.

improve their governance practise by implementing mechanisms and reform strategies currently applied in the Western model.⁷⁵³

Nevertheless, no matter how high the ethical standards of any individual, there will always be exceptions.⁷⁵⁴ As Hirschman emphasises,⁷⁵⁵

Under any economic, social, or political system, individuals, business firms, and organizations in general are subject to lapses from efficient, rational, law-abiding, virtuous, or otherwise functional behaviour. No matter how well a society's basic institutions are devised, failures of some actors to live up to the behaviour which is expected of them are bound to occur.⁷⁵⁶

Therefore, extra measures must be taken to protect the public interest. There are many examples cited in early Islamic history where rulers were subjected to accountability by the Prophet and the first four Caliphs, despite being regarded as role models in their time and for future Muslim generations. In particular, the second Caliph Umar Ibn Al-Khattab (ruled 634–644 CE) held some of his governors to public accountability, regardless of their status as prominent and pious Companions of the Prophet Muhammad.⁷⁵⁷

Accordingly, subjecting SSB members to accountability should not be perceived as showing less respect to Shari‘ah scholars or doubting their credibility, but rather dealing professionally with an essential group in the industry and adding a layer of protection for public interest. This is particularly important if the IIFS is operating in a global market where the local reputation of the Shari‘ah board members’ reliability

⁷⁵³ Ibid.

⁷⁵⁴ Historically, these individuals are known as *ulama-e soo* (vicious scholars or hypocrite scholars) who would circumvent the teaching of Shari‘ah in order to protect their interests or the rulers’ interest or to provide justification for their wrongdoing. See Moinuddin Ahmed, *Ulama : the Boon and Bane of Islamic Society* (New Delhi: Kitab Bhavan, 1990), p77; Ghazzali, *The Book of Knowledge; Ihya`ulum al-din.*, trans. Nabih Amin Faris, 2nd ed. (Lahore: S.M. Ashraf, 1966), Section VI.

⁷⁵⁵ Albert O. Hirschman, *Exit, Voice, and Loyalty; Responses to Decline in Firms, Organizations, and States* (Cambridge, Mass.: Harvard University Press, 1970), p1.

⁷⁵⁶ Ibid.

⁷⁵⁷ See, for example, the stories of Caliph Umar with the following Companions: Saad Bin Waqas, Khalid Bin Waleed, Said ibn Aamir, and Amr ibn al-Aas. See Mian Usman, "The Islamic Concept of Leadership," Allvoices, Inc, <http://www.allvoices.com/contributed-news/4804200-the-islamic-concept-of-leadership>. accessed 9 August 2011; Badr ‘Abd al-Ḥamīd Hmīṣah, "Muḥāsabah al-Wulāh " Ṣayd al-Fawā’id <http://www.saaaid.net/Doat/hamesabadr/205.htm>. accessed 9 August 2011

may not be sufficient to allay stockholder suspicions over the SSB's lack of accountability.

5.4.4. SSBs' Lack of Transparency

One of the main criticisms directed at IIFS is their general lack of transparency, particularly in relation to Shari'ah governance. Although transparency is regarded as an essential element of modern corporate governance,⁷⁵⁸ it does not seem to be common practise among Islamic financial institutions, which operate in a less transparent environment than do conventional financial institutions.⁷⁵⁹

Wilson⁷⁶⁰ notes that regulators and official bodies in Muslim countries tend to deal with Islamic finance issues as a sensitive subject and do not expose them to public view. This is because the governors of central banks are careful not to be seen taking action which violates Shari'ah principles.⁷⁶¹ In addition, severe competition in the industry might block the disclosure of details of innovative Islamic financial products. The reliability of the transaction is not based on the level of transparency and disclosure, but rather on people's acceptance and trust of the Shari'ah scholar who has approved the product.⁷⁶²

Furthermore, the subject has received little attention in the AAOIFI standards and guidelines.⁷⁶³ For instance, AAOIFI's recommendations for the contents of an SSB annual report are superficial and disregard the disclosure of important information. Neither does the standard promote revealing key information about IIFS Shari'ah board members, such as membership duration, procedures for selection and

⁷⁵⁸ Benjamin E. Hermalin and Michael S. Weisbach, "Transparency and Corporate Governance," (2007) http://www.law.yale.edu/documents/pdf/cbl/HW_mkts_v5.pdf accessed 28 August 2011

⁷⁵⁹ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services"; Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p88; Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

⁷⁶⁰ Wilson, "Regulatory Challenges Posed by Islamic Capital Market Products and Services," p20.

⁷⁶¹ Ibid.

⁷⁶² Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

⁷⁶³ Khorshid, "Shariah Board Accountability".

reappointment, or qualifications and professional background.⁷⁶⁴ Moreover, as with members of a board of directors, SSB members' financial rewards and their work affiliations with other financial institutions (including the number of SSBs they serve) should be revealed.⁷⁶⁵

Most importantly, stakeholders should be made aware of the SSB's duties, the legal power of its decisions (whether binding or advisory in nature), and the process of Shari'ah supervision and decision-making. Some IIFS are advertised as completely under the supervision of the Shari'ah board, while their SSB in practise only conducts *ex ante* Shari'ah review.⁷⁶⁶ Other institutions claim to have an internal Shari'ah review unit while, in fact, they only have one officer responsible for auditing its branches.⁷⁶⁷ Besides, it is important to disclose how SSBs collect their data. Most SSBs state that a sample of IIFS transactions has been examined without saying when or revealing how much this sample represents the IIFS business operations.⁷⁶⁸

Another important point is that IIFS should disclose the disposal of non-Shari'ah compliant income.⁷⁶⁹ Shareholders need to know how much of the IIFS operations this income represents, and whether it was correctly distributed. Many SSB reports state that IIFS operations were fully Shari'ah compliant without referring to the percentage of non-Shari'ah compliant earnings that must inevitably be generated in practise.⁷⁷⁰

⁷⁶⁴ Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

⁷⁶⁵ Fidād, "al-Raqābah al-Shar'iyyah Wa Dawruhā Fī Ḍabṭ A'māl al-Maṣārif al-Islāmiyyah," p19.

⁷⁶⁶ al-Hītī, "Athar al-Raqābah al-Shar'iyyah 'alā Ail-tizām al-Maṣārif al-Islāmiyyah bi-al-'Aḥkāmī al-Shar'iyyah " p21-25.

⁷⁶⁷ 'Ādil 'AbdAllāh Bāryān, "Asālīb Taf'īl Dawr al-Raqābah al-Shar'iyyah Fī al-Maṣārif al-Islāmiyyah", p35.

⁷⁶⁸ al-Sa'ad, "al-Raqābah al-Shar'iyyah Wa' Atharhā Fī al-Maṣārif al-Islāmiyyah," p15-19; al-Ṭayyib, "Taqyīm al-Raqābah al-Shar'iyyah fī Ḍil al-Nizām al-Maṣrifī al-Islāmī al-Shāmil," p27; 'Abd al-Razzāq Raḥīm al-Hītī, "Athar al-Raqābah al-Shar'iyyah 'alā Ail-tizām al-Maṣārif al-Islāmiyyah bi-al-'Aḥkāmī al-Shar'iyyah " (ibid.31/5/2009 - 3/6/2009), p21.

⁷⁶⁹ Muḥammad 'Alī Yūsuf Ahmad, "Dawr al-Suluṭāt al-Riqābiyyah Fī al-Riqābah 'Alā al-Mu'assasāt al-Māliyyah al-Islāmiyyah " (paper presented at the The 2nd Conference of Islamic Financial Services., Tripoli-Libya, 27-28/4/2010), p19.

⁷⁷⁰ Ahmad al-Islāmbūlī, "Dawr al-Hay'āt al-Shar'iyyah Fī Ḍabṭ A'māl al-Mu'assasāt al-Māliyyah al-Islāmiyyah " (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009), p19.

The following indices that I have compiled compare Shari‘ah supervision disclosure in 12 Saudi banks⁷⁷¹ along with nine UK banks⁷⁷² offering Islamic financial services

⁷⁷¹ Source of date: information posted on the websites and annual reports of the following banks: Alrajhi Bank, "The Sharia Group"; "Annual Report 2010," Alrajhi Bank, <http://www.alrajhibank.com.sa/en/media-centre/reports/Documents/annual-report2010-en.pdf>. accessed 28 August 2011; Bank Albilad, "Sharia Board," <http://www.bankalbilad.com/ar/shariah.asp>, <http://www.bankalbilad.com/en/shariah.asp>. accessed 28 August 2011; "Financial Statements for 2010," <http://www.bankalbilad.com/en/BILAD31-12-2010.pdf>. accessed 28 August 2011; Alinma Bank, "Shariah Board," http://www.alinma.com/wps/portal/alinma!/ut/p/c5/04_SB8K8xLLM9MSSzPy8xBz9CP0os3hzf2cLDy93A0t3d1c3A093Ixd3_yBfI29TA_3g1Dz9gmxHRQA7laOC/. accessed 28 August 2011; "Annual Report 2010," Alinma Bank,, http://www.alinma.com/wps/wcm/connect/512dd680467a8afb930ebb690642abc7/Alinm_annual_report_2010_eng%28may22%29+22.5.11.pdf?MOD=AJPERES&CACHEID=512dd680467a8afb930ebb690642abc7. accessed 28 August 2011; Bank AlJazira (BAJ), "Corporate Profile," <http://www.baj.com.sa/about-us.aspx?page=corporate-profile&id=139>. accessed 28 August 2011; "Annual Report," <http://www.baj.com.sa/pdf/Baj%20Annual%20Report%20English.pdf>. accessed 28 August 2011; The National Commercial Bank, "Annual Report " http://www.alahli.com/en-US/About%20Us/News_Reports/Documents/Reports%202010/NCB%20AR10%20English.pdf. accessed 28 August 2011; "The NCB Shariah Board " <http://www.alahli.com/ar-SA/About%20Us/ibdG/Pages/TheNCBShariahBoard.aspx>. accessed 28 August 2011; Saudi Hollandi Bank (SHB), "Shari‘ah Board Members," <http://shb.com.sa/en/about/AboutSHB/ShariahBoardmembers.aspx>. accessed 28 August 2011; Saudi Hollandi Bank(SHB), "Annual Report " http://www.shb.com.sa/PDF/SHB%20Annual%20Report%202010_English.pdf. accessed 28 August 2011; SAMBA, "Islamic Products," Samba Bank, http://www.samba.com/ENGLISH/CONSUMER/HTML/CONSISLAMICPRODUCTS_01_01_en.html. accessed 28 August 2011; "Annual Reports," Samba Bank, http://www.samba.com/English/Common/HTML/abtSambaFReports_01_01_en.html. accessed 28 August 2011; Riyadh Bank, "Islamic Banking " <http://www.riyadbank.com/English/PersonalBanking/IslamicBanking.html>. accessed 28 August 2011; "Annual Report," Riyadh Bank, <http://www.riyadbank.com/PDF/reports/annualreports/en/2010/AnnualReport2010.pdf>. accessed 28 August 2011; Bank Saudi Fransi (BSF), "Islamic Finance " <http://www.alfransi.com.sa/en/article/corporate-services/corporate-banking/islamic-finance.html>. accessed 28 August 2011; "Annual Report," <http://www.alfransi.com.sa/en/general/download/file/1369>. accessed 28 August 2011; Arab National Bank (ANB), "Islamic Banking Division Profile," http://www.anb.com.sa/about_islamic.asp. accessed 28 August 2011; "Annual Report," http://www.anb.com.sa/pdf/Reports/2010/ANB_English_review.pdf. accessed 28 August 2011; SABB, "Shariah Committee," SABB Bank, http://www.sabb.com/1/2/sabb-en/about-us/profile/sahariah_advisory_committee. accessed 28 August 2011; "Annual Report," SABB Bank http://www.sabb.com/1/PA_1_083Q9FJ08A002FBP5S00000000/content/SABB/en/about_us/attachments/annual_reports/sabb_annual_report_2010_en.pdf. accessed 28 August 2011; The Saudi Investment Bank (SAIB), "Islamic Banking," <http://www.saib.com.sa/english/islamic.aspx>. accessed 28 August 2011; "Financial Statements," <http://www.saib.com.sa/Docs/Financial%20Statements%202010%20English.pdf>. accessed 28 August 2011

⁷⁷²Source of data: information posted on the websites and annual reports of the following banks: Islamic Bank of Britain (IBB), "Sharia Supervisory Committee," <http://www.islamic-bank.com/sharia-finance/sharia-supervisory-committee/>. accessed 28 August 2011; Islamic Bank of Britain IIBI, "Annual Report and Financial Statements " <http://www.islamic-bank.com/GetAsset.aspx?id=fAAzADkANgB8AHwAVABYAHUAZQB8AHwAMAB8AA2>. accessed 28 August 2011; Ahli United Bank (UK) (AUB), "Our Sharia'h Board " www.iibu.com/shariaa_board/sboard.aspx. accessed 28 August 2011; "Annual Report," http://www.ahliunited.com/pdfs/ar/AUB_AnnualReport_2010.pdf. accessed 28 August 2011; HSBC

(see Table 1 and Table 2). They show the average disclosure and the desirable disclosure in the following areas: SSB composition, Shari‘ah scholars’ professional background, affiliation with other SSBs, SSB members’ financial rewards, the SSB annual report to shareholders, the publication of *fatwas* or decisions, SSB duties, SSB decision power (binding or advisory), supervision processes, and selection procedures (by shareholders, the board of directors, or banking management).

As the average results of the two countries show, a transparency culture in banks offering Islamic financial services seems to be more prevalent in the UK than in Saudi, although the UK is a secular country with minority Muslim population and Saudi is an Islamic country. IIFS in the UK are in a better position with regard to disclosing Shari‘ah scholars’ membership in other SSBs. These countries’ political systems might have influenced this outcome, since unlike the absolute monarchy in Saudi,⁷⁷³ the democratic system of the UK promotes transparency. Besides, professional banking practises were established a long time ago in the UK, and modern corporate governance originated in the West.⁷⁷⁴ Nevertheless, the disclosure of SSB remuneration appears to be a sensitive subject in both countries, to the extent that it has never been revealed. Lastly, the indices show that, despite the benefits of

Amanah, "Shariah Supervision," <http://www.hsbcamanah.com/amanah/about-amanah/islamic-banking/shariah-supervision>. accessed 28 August 2011; United National Bank, "Islamic Products," <http://www.unbankltd.com/islamic-products/>. accessed 28 August 2011; ABC International Bank plc (ABCIB), "Shariah Compliance," ABCIB,, http://www.alburaq.co.uk/shariah_compliance.asp. accessed 28 August 2011; Lloyds TSB, "Islamic Business Bank Account," <http://www.lloydstsbbusiness.com/accounts/islamic.asp>. accessed 28 August 2011; European Islamic Investment Bank plc's (EIIB), "Sharia Board," EIIB,, http://www.eiib.co.uk/html/sharia_board.asp. accessed 28 August 2011; "Annual Report " EIIB,, <http://www.eiib.co.uk/documents/EIIBAnnualReport2010Final.pdf>. accessed 28 August 2011; QIB(UK), "Our People " QIB Bank(UK) <http://www.qib-uk.com/html/our-people.asp>. accessed 28 August 2011; Gatehouse Bank, "Shariah Supervisory Board," <http://www.gatehousebank.com/about-us/shariah-supervisory-board/>. accessed 28 August 2011; "Annual Report," http://www.gatehousebank.com/common/documents/annual-reports/Gatehouse_Bank_Annual_Report_2009.pdf. accessed 28 August 2011

⁷⁷³ See generally, Khaled Hussainey and Ali Al-Nodel, "Corporate Governance Online Reporting by Saudi Listed Companies," in *Corporate governance in less developed and emerging economies*, ed. Matthew Tsamenyi and Shazad Uddin (Bingley: Emerald Jai, 2008), p42

⁷⁷⁴ Randall Morck and Lloyd Steier, *The Global History of Corporate Governance : an Introduction* (Cambridge, Mass.: National Bureau of Economic Research, 2005).

publishing SSB *fatwas*, such as educating the public about Islamic finance and engaging stakeholders in overseeing IIFS compliance with SSB rulings,⁷⁷⁵ very few financial institutions have taken the incentive to publish the decisions of their SSB.

Shariah Governance disclosure Indexes in KSA banks

Source: banks websites and Annual Reports

| KSA BANKS | SSB composition | Professional Background | Affiliation with other SSB | SSB financial rewards | SSB annual Report | Fatwas | SSB duties | power | Supervision Process | Selection Procedure |
|----------------------|-----------------|-------------------------|----------------------------|-----------------------|-------------------|--------|------------|-------|---------------------|---------------------|
| ALRAJHI | 1 | 0 | 0 | 0 | 0 | 1 | 1 | 1 | 1 | 1 |
| ALBILAD | 1 | 1 | 0 | 0 | 0 | 1 | 1 | 1 | 1 | 0 |
| ALINMA | 1 | 1 | 0 | 0 | 0 | 0 | 1 | 1 | 1 | 1 |
| BAJ | 1 | 0 | 0 | 0 | 1 | 0 | 1 | 1 | 1 | 0 |
| NCB | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 1 | 0 |
| SHB | 1 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| SAMBA | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| RIYAD | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 0 | 0 |
| ALFRANSI | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 0 |
| ANB | 1 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 1 | 0 |
| SABB | 1 | 1 | 0 | 0 | 0 | 0 | 1 | 0 | 0 | 0 |
| SAIB | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Average disclosure | 0.92 | 0.33 | 0.00 | 0.00 | 0.08 | 0.17 | 0.67 | 0.42 | 0.50 | 0.17 |
| Desirable disclosure | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |

Numbers are binary, 1 being disclosure and 0 being non-disclosure.

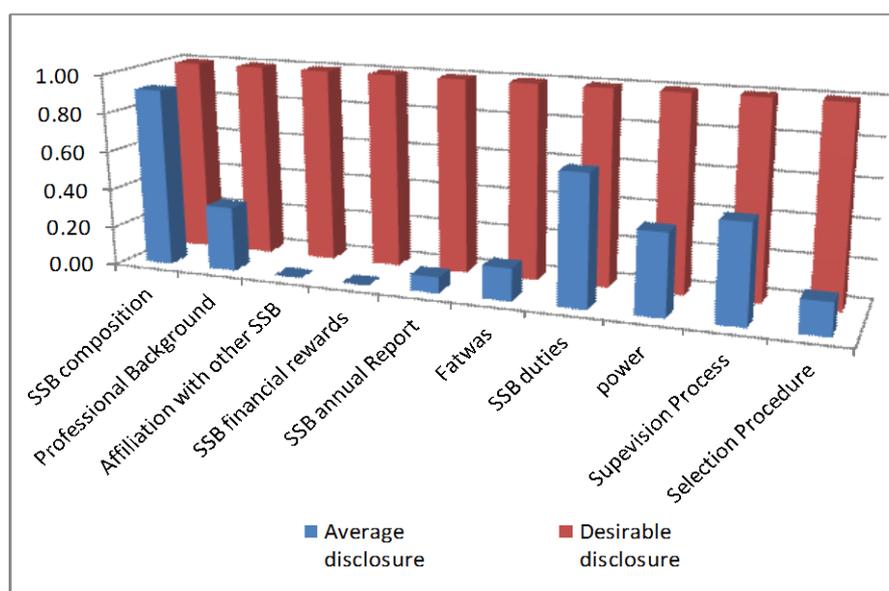


Table 1. Shariah Governance Disclosure Indexes in KSA Banks

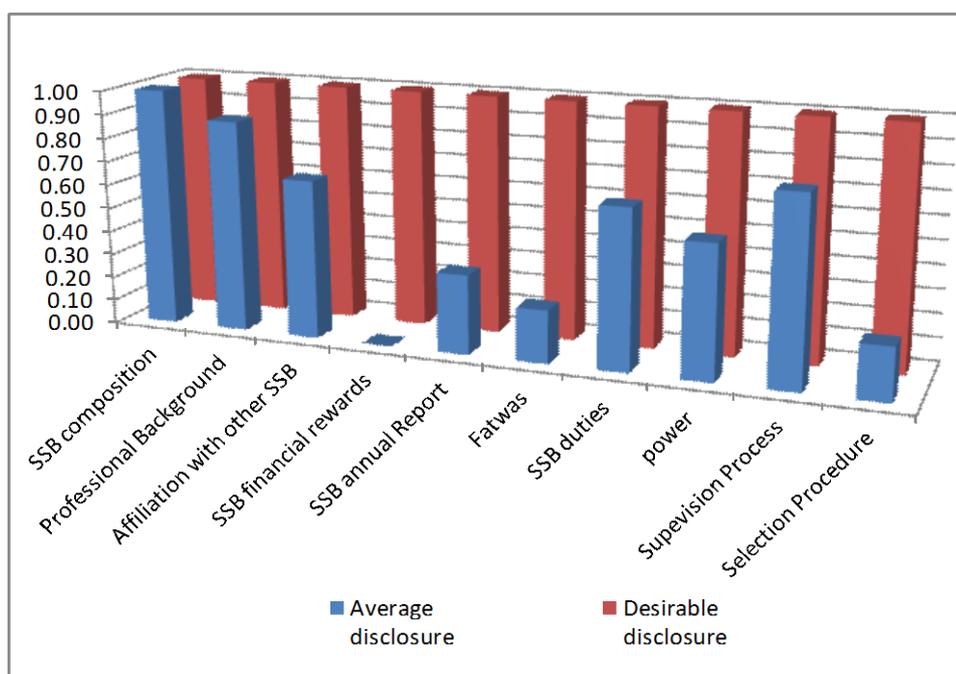
Table 2. Shari ‘ah Governance Disclosure Indexes in KSA Banks

Shariah Governance disclosure Indexes in UK banks

Source: banks websites and Annual Reports

| UK BANKS | SSB composition | Professional Background | Affiliation with other SSB | SSB financial rewards | SSB annual Report | Fatwas | SSB duties | power | Supervision Process | Selection Procedure |
|-----------------------------|-----------------|-------------------------|----------------------------|-----------------------|-------------------|--------|------------|-------|---------------------|---------------------|
| IBB | 1 | 1 | 1 | 0 | 1 | 1 | 1 | 1 | 1 | 0 |
| AUB UK | 1 | 1 | 1 | 0 | 0 | 0 | 1 | 1 | 1 | 0 |
| HSBC Amanah | 1 | 1 | 1 | 0 | 0 | 0 | 1 | 1 | 1 | 0 |
| UNB | 1 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 0 |
| Alburaq | 1 | 1 | 1 | 0 | 0 | 1 | 1 | 0 | 1 | 0 |
| Lloyds TSB- | 1 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| EI | 1 | 1 | 1 | 0 | 1 | 0 | 1 | 1 | 1 | 1 |
| QJB (UK) plc | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Gatehouse Bank | 1 | 1 | 1 | 0 | 1 | 0 | 1 | 1 | 1 | 1 |
| Average disclosure | 1.00 | 0.89 | 0.67 | 0.00 | 0.33 | 0.22 | 0.67 | 0.56 | 0.78 | 0.22 |
| Desirable disclosure | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |

Numbers are binary, 1 being disclosure and 0 being non-disclosure.



5.4.5. *The Lack of Independence of SSBs*

Independence, according to *Oxford Dictionary of English*, is the state of being “free from outside control; not subject to another's authority”.⁷⁷⁶ Any factor that compromises the independence of fiduciaries (such as directors, agents, and external auditors) will affect their judgment, reliability and public confidence.⁷⁷⁷ However, the standard of independence and acting in a good faith as a fiduciary duty can vary from one profession to another.⁷⁷⁸ Contemporary Islamic finance literature seems to offer a similar but less strict mindset posed in guidelines and codes issued by accounting and auditing regulatory and professional bodies.⁷⁷⁹ Al-Khalīfī, for example, defines the independent authority of SSBs as a way of exercising their functions impartially and in complete freedom. They should not be influenced by any kind of pressure, whether from IIFS management or shareholders, that may negatively affect their decisions.⁷⁸⁰

Al-Shabīlī⁷⁸¹ outlines three elements of SSB independence. The first is employment independence: the external Shari‘ah supervisor should not be an employee of the IIFS, but should be appointed from outside the IIFS staff. In addition, the level of the internal Shari‘ah department in the IIFS structure should be

⁷⁷⁶ Stevenson, "Oxford Dictionary of English".

⁷⁷⁷ Zabihollah Rezaee, *Corporate Governance and Ethics* (Hoboken, NJ: John Wiley & Sons, 2009), p270.

⁷⁷⁸ See generally: Gerard M. D. Bean, *Fiduciary Obligations and Joint Ventures :The Collaborative Fiduciary Relationship* (Oxford; New York, N.Y.: Clarendon Press, 1995), p27-35; Robert A. Pearce, John Stevens, and Warren Barr, *The Law of Trusts and Equitable Obligations* (Oxford; New York: Oxford University Press, 2010), p909-15; Martha Bruce, *Rights and Duties of Directors* (London: Tolley Publishing Co Ltd, 2002), p42-49.

⁷⁷⁹ Most guidelines and codes issued by regulatory and professional bodies highlight two notions of auditor independence: independence in fact (or mind) and independence in appearance. The former requires auditors to have a state of mind that is not influenced by any factors which may affect professional judgment. An auditor must be able to perform the task with honesty, impartiality and “professional scepticism.” The latter requires auditors to avoid any significant facts or situations that might result in a reasonable conclusion on the part of an informed third party that the auditor’s honesty, impartiality, or “professional scepticism” has been affected. Christiane Strohm, *United States and European Union Auditor Independence Regulation: Implications for Regulators and Auditing Practice* (Wiesbaden: Deutscher Universitäts-Verlag, 2006), p18.

⁷⁸⁰ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p26.

⁷⁸¹ al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif:Ḍawābiḥā Wa Aḥkāmā Wa Dawrhā fi Ḍabṭ ‘Amal al-Maṣārif," p20.

sufficient to accomplish its responsibilities. It should not be lower than the level of the internal audit unit, which should report directly to the SSB, not to the management of the bank. The second element is financial independence, which is achieved when an SSB member's fee is not determined by the number of products or contracts he has approved, but according to the effort he has made in conducting such a job. In the case of internal Shari'ah auditors, financial independence is achieved by ensuring that their remuneration is not linked with the content of their reports. The third element is independence in appointment and dismissal. The SSB member must be appointed by the highest authority in the IIFS, which is the annual general meeting (AGM) of shareholders. The internal Shari'ah auditor can be appointed and dismissed by an administrative decision, subject to the approval of the SSB.

In theory, Shari'ah Board members have an obligation to provide an impartial report on any breach of Islamic law that takes place within an Islamic financial institution. However, the existence of two boards in the IIFS structure, with the board of directors having a superior power over an SSB, may cause a serious conflict of interest. The fact that the IIFS board or management can appoint, dismiss, or fix the remuneration of the SSB member leaves the door open for IIFS management to use such leverage to influence Shari'ah board judgments. For instance, the board of directors may try to pressure the SSB to issue a *fatwa* approving a certain product or service to maximise the IIFS profit, regardless of its compliance with Shari'ah principles. Or they might threaten SSB members with termination of their contracts to prevent them from reporting non-Shari'ah compliant activities, which is likely to shake stakeholders' confidence.⁷⁸²

⁷⁸² Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services"; Siti Faridah Abd Jabbar, "The Sharia Supervisory Board of Islamic Financial Institutions: A Case for Governance," *The Company Lawyer* 30, no. 8 (2009): p244; Abdul-

In the context of Shari‘ah supervision, five factors can possibly compromise SSB independence,⁷⁸³ namely, the approach to appointments, high remuneration, the provision of credit facilities to SSB members, ownership of shares in the IIFS, and the holding of an executive position.

5.4.5.1. The Approach to Appointments

The Islamic finance industry has no standard practise for appointing Shari‘ah advisors. Generally, SSB members are appointed either directly by the IIFS board of directors or management, or else in the annual general meeting of shareholders. It is not clear which method is the most popular in the industry. According to a study conducted by Bahjat⁷⁸⁴ on sixteen Islamic institutions, only seven SSBs have ever been appointed at an AGM. Five were appointed by a board of directors, and it was not clear which method was used for appointing the members of the remaining four SSBs. In another study, Hussain Hamed Hassan,⁷⁸⁵ a prominent international Shari‘ah

Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p79.

⁷⁸³ External auditors' independence, to which some Islamic finance literatures make reference (HH Hassan, 'al'elaqah beyn alhey'eat alesher'eyh w alemraj'eyen alekharejyen' Accounting and Auditing Organization for Islamic Financial Institutions AAOIF), can be compromised by several threats. The Ethical Standards issued by The Auditing Practices Board (APB) in addition to The International Federation of Accountants (IFAC) Code of Ethics for Professional Accountants identify six general threats: self-interest, self-review, advocacy, familiarity or trust, management, and intimidation. The threat of self-interest is found when an auditor hesitates to act independently because it may endanger his interests (for example, shares in the audited institution). The threat of self-review occurs when an auditor provides a non-auditing service to be incorporated in the financial statement. The threat of advocacy appears when an auditor plays the role of an advocate to an audited company which requires him to adopt a position in support of that taken by the management. The threat of familiarity or trust can emerge when an auditor does not sufficiently question the point of view of the audited company. A common example is where a close personal relationship has developed with the staff of the audited entity. Moreover, a management threat can occur when an auditor makes a decision on behalf of the administration of the audited financial institution. This usually takes place when an audited entity asks the audit firm to provide non-audit services that will influence judgments made by the management. Finally, the intimidation threat occurs when the performance of an auditor is affected by fear or menaces. This could be the situation when an auditor deals with aggressive and controlling management. See: Brenda Porter, David J. Hatherly, and Jon Simon, *Principles of External Auditing* (Chichester, England: John Wiley, 2008), p104-06.

⁷⁸⁴ Muḥammad Fu'ād Bahjat, "Naḥw Mi'yār Lil-rriqābah al-Shar'īyyah Fī al-Bunūk al-Islāmiyyah," *Journal of King Abdulaziz University: Islamic Economics* 3, no. 2 (1994). Cited in Fayṣal 'Abd al-'Azīz Farāḥ, "al-Raqābah al-Shar'īyyah al-Wāqī' Wa al-Mithāl " (paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/06/2005), p26.

⁷⁸⁵ Hassan, "al-'Alāqah Bayn al-Hay'āt al-Shar'īyyah wa al-murāji'īn al-khārijīyyīn " p9.

scholar, suggests that 89% of the SSBs in IIFS are appointed by a board of directors and 11% are appointed at an AGM.

The first method, appointment by the board of directors, is associated with two issues. First, the board may use its leverage to influence SSB decisions. Given that the board usually represents big shareholders in an institution, such pressure is likely to be used to protect any financial interests. The danger is greater in cases where there is only a single Shari'ah advisor in the institution. The second issue is the lack of objectivity in selecting SSB members. This is because board members tend to choose scholars with whom they have personal or friendly relationships.⁷⁸⁶ Such familiarity can be an impediment for SSBs when endeavouring to perform their task in a professional manner.⁷⁸⁷

Although appointing SSBs in the shareholders' AGM is thought to boost SSB independence,⁷⁸⁸ and although it represents the current practise supported by AAOIFI standards, this method is also not without its flaws. This is because the board of directors recommends the appointment of certain individuals at general meetings, and these recommendations are usually approved without objection.⁷⁸⁹ Board recommendations tend to be influenced by management views. Therefore, it is unlikely to assume that IIFS management will have no power over the selection of SSBs appointed in an AGM.

Furthermore, even where shareholders directly make the selections, the decisions of the AGM can be influenced by a few individuals who control the majority of a

⁷⁸⁶ Qaṭṭān, "Hay'ah al-Raqābah al-Shar'īyyah Akhtiyār A'ḍā'ihā Wa Ḍawābiḥā " p20.

⁷⁸⁷ 'Abd al-Majīd Maḥmūd al-Ṣalāḥīn, "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Wa Dawruhā Fī al-Maṣrifīyyah al-Islāmiyyah " (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005), p257.

⁷⁸⁸ Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* p55.

⁷⁸⁹ Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

company's shares.⁷⁹⁰ This might be the case in both private and government companies which become publicly traded in the stock market. For example, Al Rajhi Bank, the largest Saudi Islamic bank and the second biggest Islamic bank in the world, was listed in the Saudi stock market in 1988.⁷⁹¹ However, the Al Rajhi family holds a majority share in the company, and family members occupy six out of the 11 seats on the board of directors. These include the chairman of the board and his son, who is the Chief Executive Officer (CEO). In this example, the CEO will likely have a major influence on his father, as well as on the rest of the family members on the board. Therefore, it is unrealistic to claim that selecting SSB members in the AGM, which is the norm in Al Rajhi Bank, is sufficient to provide autonomy for SSB members.⁷⁹²

Another criticism directed at this method is that it prevents investment account holders from participating in the selection of SSBs.⁷⁹³ Unlike conventional banks, investment account holders in Islamic finance are affected by SSB selections because they share profit and risk with the institution. Therefore, they should be involved in the process of SSB appointment.

To avoid such limitations, some experts have suggested that a regulatory body oversee the selection of SSB members in the AGM.⁷⁹⁴ This would provide another layer to protect SSB independence from the board of directors' influence. It would

⁷⁹⁰ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p79 n13; al-Hītī, "Athar al-Raqābah al-Shar'īyyah 'alā Ail-tizām al-Mašārīf al-Islāmiyyah bi-al-'Aḥkāmī al-Shar'īyyah " p32.

⁷⁹¹ Alrajhi Bank, "About Us," <http://www.alrajhibank.com.sa/AboutUs/Pages/default.aspx>. accessed 18 April 2011

⁷⁹²The board members' names as they appeared on the bank website on 18/04/2011, *ibid*.

⁷⁹³ Qaṭṭān, "Hay'at al-Raqābah al-Shar'īyyah Akhtiyār A'ḍā'ihā Wa Ḍawābiḥā " p10; 'Abd al-Hādī Ḥabṭūr, "Hay'at Riqābiyyah Shar'īyyah fī al-Mašārīf al-IslāmiyyahTa'mal k " Muassasāt Khayriyyat " Dūn Ṣifah Qānūniyyah ", *al-Āqṭiṣādiyyah*, 20 June 2010 http://www.aleqt.com/2010/06/20/article_408864.html. accessed 20 October 2010

⁷⁹⁴ al-Ṣalāhīn, "Hay'at al-Fatwā Wa al-Riqābah al-Shar'īyyah Wa Dawruhā Fī al-Mašrifīyyah al-Islāmiyyah " p258; Ṭah Muḥammad Fāris, "Ḍawābiḥ Wa Āliyyāt Akhtiyār A'ḍā' Hay'at al-Fatwā Wa al-Riqābah al-Shar'īyyah Fī al-Mu'asasāt al-Māliyyah " (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5- 3/6/2009), p48-51.

also ensure greater objectivity in selecting SSB members. Such a practise is already applied in the United Arab Emirates (UAE)⁷⁹⁵ as well as in Malaysia,⁷⁹⁶ where Islamic banks are required to submit the names of SSB candidates to a supreme Shari‘ah board for final approval. However, this mechanism cannot be applied at the present time in countries such as Saudi Arabia, owing to the absence of regulations of Islamic finance, or in countries such as the UK, where a secular system is applied and the regulator will not interfere in a religious matter.⁷⁹⁷

Another suggestion is to refer the issue of SSB member selection to an international body funded by charity, which would comprise globally recognised scholars capable of assessing the competence of potential candidates.⁷⁹⁸ However, it is questionable whether financial institutions would voluntarily adhere to the control of such a body. Unless it were backed by central banks, it could be problematic for a cross-border financial institution to operate in countries with different approaches towards Islamic finance.

5.4.5.2. High Remuneration

Classical Islamic scholars have always stressed the importance of the independence of the *muftī* (a scholar who provides a Shari‘ah answer) from the *mustaftī* (an individual who asks the question).⁷⁹⁹ Initially, classical *fiqh* jurists debated whether it was permissible for the *muftī* to receive payment from individuals in exchange for answering a religious question.⁸⁰⁰ Proponents of prohibiting this

⁷⁹⁵ "Federal Law No-(6) of 1985 concerning Islamic Banks and Financial Institutions and Investment Companies". Article 6. See also: al-Ṣalāhīn, "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyah Wa Dawruhā Fī al-Maṣrifīyah al-Islāmiyyah " p258; Qaṭṭān, "Hay'ah al-Raqābah al-Shar'iyah Akhtiyār A'dā'ihā Wa Ḍawābiḥā " p10.

⁷⁹⁶ Bank Negara Malaysia (BNM), "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p29.

⁷⁹⁷ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*, p13.

⁷⁹⁸ Laldin, "Dawr al-Raqābah al-Shar'iyah Fī Dabṭ a'māl al-Maṣārif al-Islāmiyyah," p10.

⁷⁹⁹ Bāryān, "Asālib Taf'īl Dawr al-Raqābah al-Shar'iyah Fī al-Maṣārif al-Islāmiyyah " p26-30.

⁸⁰⁰ While it is allowed within the Maliki, Shafi'i and minority Hanbali schools of thought, it is not lawful under the Hanafi and mainstream Hanbali schools of thought. See: al-Shabīlī, "al-Raqābah al-

remuneration argue that allowing such a practise would endanger the scholar's autonomy, since the Shari'ah ruling may not be in favour of the individual. Consequently, as with judges and governors, the remuneration of scholars who provide a *fatwa* for the public should be paid by the Islamic state like any other public servant.

However, it is unlikely that this debate applies to the current nature of SSB work. There is a major difference between answering general questions from the public, as discussed in the classical literature, and between ensuring Shari'ah compliance in a private financial institution. The latter is an unprecedented situation for Shari'ah scholars. It takes greater effort and more time, requiring scholars to review product documents and develop an understanding of complex financial instruments. Hence, most contemporary jurists hold the view that it is religiously lawful for Shari'ah scholars to accept remuneration in exchange for time and effort provided to ensure Shari'ah compliance.⁸⁰¹

Nevertheless, the phenomenon of employing a "private scholar" in financial institutions has not gone without criticism from some official scholars appointed by the state.⁸⁰² They have argued that such a practise has negatively resulted in a so-called "*fatwa* shopping" situation, where some SSB members use jurisprudential ruses to offer resolutions that are tailored to suit the desires of the IIFS, although doing so could undermine the spirit of Islamic finance.⁸⁰³ In the eyes of these critics, banks are

Shar'iyah 'Alā al-Maṣārif: Dawābiṭhā Wa Aḥkāmhā Wa Dawrhā fī Ḍabṭ 'Amal al-Maṣārif," p8-9; Fāris, "Dawābiṭ Wa Āliyyāt Akhtiyār A'ḍā' Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyah Fī al-Mu'asasāt al-Māliyyah " p31-34.

⁸⁰¹ al-Shabīlī, "al-Raqābah al-Shar'iyah 'Alā al-Maṣārif: Dawābiṭhā Wa Aḥkāmhā Wa Dawrhā fī Ḍabṭ 'Amal al-Maṣārif," p9; Fāris, "Dawābiṭ Wa Āliyyāt Akhtiyār A'ḍā' Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyah Fī al-Mu'asasāt al-Māliyyah " p32; Laldin, "Dawr al-Raqābah al-Shar'iyah Fī Ḍabṭ a'māl al-Maṣārif al-Islāmiyyah," p10; Ḥamzah 'Abd al-Karīm Ḥammād, *al-Raqābah al-Shar'iyah Fī al-Maṣārif al-Islāmiyyah* (Amman: Alinvaais, 2006), p120.

⁸⁰² Warde, *Islamic Finance in The Global Economy*, p227-228.

⁸⁰³ Ibid.

using their clients' money to pay a high remuneration to SSB members in exchange for rulings with doubtful religious validity.

It is probably the reports of high remuneration paid to some of the most popular Shari'ah supervisors in the industry that provoked criticism on this issue. With no standard practise in IIFS,⁸⁰⁴ it seems to be important to address who should determine SSB remuneration and how it should be calculated. According to a study conducted by Abumouamer,⁸⁰⁵ for 75% of IIFS in the industry, SSB remuneration is decided by shareholders in their AGM; the board of directors determines it for 15.6%, and IIFS management fixes it for 9.4%. The calculation method varies from one IIFS to another. Some IIFS pay an annual or a monthly fee according to a set number of board meetings. Others pay a percentage of the bank's overall profit.⁸⁰⁶ The latter is the case with Faisal Islamic Bank of Egypt, where SSB and board of directors remuneration is fixed in the annual budget to be between 5% and 10% of actual profit.⁸⁰⁷ However, such a practise can severely endanger SSB independence and raise a serious conflict of interest. This is because the higher the profit, the higher remuneration SSB members receive. For instance, if this method were followed by Al Rajhi Bank, which made SR 6,767 million in net profit in 2009,⁸⁰⁸ assuming that the total number of board of directors and SSB members is 15, with their remuneration set at 8% of the actual profit, each member would receive about SR 36 million.

A related discussion in this regard is whether a Shari'ah supervisor can receive a percentage of the revenue from a product approved by the SSB. Some scholars argue

⁸⁰⁴ Laldin, "Dawr al-Raqābah al-Shar'īyyah Fī Ḍabṭ a' māl al-Maṣārif al-Islāmiyyah," p9.

⁸⁰⁵ Abumouamer, "An Analysis of the Role and Function of the Shariah Control in Islamic Banks," p266. Compare with Farah, "al-Raqābah al-Shar'īyyah al-Wāqī' Wa al-Mithāl " p33.

⁸⁰⁶ Laldin, "Dawr al-Raqābah al-Shar'īyyah Fī Ḍabṭ a' māl al-Maṣārif al-Islāmiyyah," p9.

⁸⁰⁷ al-Ṣalāhīn, "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Wa Dawruhā Fī al-Maṣrifīyyah al-Islāmiyyah " p264; al-Islāmbūlī, "Dawr al-Hay'āt al-Shar'īyyah Fī Ḍabṭ A' māl al-Mu'asasāt al-Māliyyah al-Islāmiyyah " p7.

⁸⁰⁸ Alrajhi Bank, "2009 Annual Report," Alrajhi Bank, <http://www.alrajhibank.com.sa/reports/Pages/default.aspx>. accessed 10 March 2011

this is religiously prohibited, as it may cast suspicions over the validity of the *fatwa*.⁸⁰⁹ This is because IIFS use SSB judgment as a testimony endorsing the product in question as Shari‘ah compliant, and Islamic law does not accept testimony when a witness directly benefits from it. Given that SSBs are only paid when a product is approved, the more products they approve, the more profit they will make. However, Al-Shabīlī makes one exception,⁸¹⁰ where the product is the innovation of a Shari‘ah advisor. He argues that since Shari‘ah also protects intellectual property, these advisors have the right to receive a percentage of the profit, provided that the product is approved by other SSB members.

To limit the threat of high remuneration, Bahjat⁸¹¹ suggests issuing guidelines for the SSB fee, which would take into account the effort of the task and the average income in the country. Abumouamer⁸¹² suggests that SSB remuneration should be set by an international body such as the General Council for Islamic Banks and Financial Institutions. Such measures would help to standardise the SSB fee and protect the independence of its members.

5.4.5.3. *Credit Facility*

Another important issue that should be addressed is whether SSB members can receive credit facilities from the IIFS for which they are reviewing products. Apart from IIFS in Syria⁸¹³ and Qatar, to a limited extent, there are no restrictions on SSB members engaging in such relationships, despite the threat to Shari‘ah supervisors’

⁸⁰⁹ al-Šāliḥ, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Mašārif al-Islāmiyyah " p18. Yūsuf ‘AbdAllāh al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Mašārif:Ḍawābiḥā Wa Aḥkāmḥā Wa Dawrhā fī Ḍabṭ ‘Amal al-Mašārif" (ibid.), p9-10.

⁸¹⁰ "al-Raqābah al-Shar‘iyyah ‘Alā al-Mašārif:Ḍawābiḥā Wa Aḥkāmḥā Wa Dawrhā fī Ḍabṭ ‘Amal al-Mašārif," p9-10.

⁸¹¹ Bahjat, "Naḥw Mi‘yār Lil-rriqābah al-Shar‘iyyah Fī al-Bunūk al-Islāmiyyah." Cited in Farāḥ, "al-Raqābah al-Shar‘iyyah al-Wāqi‘ Wa al-Mithāl " p26.

⁸¹² Abumouamer, "An Analysis of the Role and Function of the Shariah Control in Islamic Banks," p266. Compare with Farāḥ, "al-Raqābah al-Shar‘iyyah al-Wāqi‘ Wa al-Mithāl " p33.

⁸¹³ Monetary and Credit Council [MCC], "Admission Rules of SSB of Islamic Banks Operating in The Syrian Arab Republic 404, MN, B4," <http://www.banquecentrale.gov.sy/mone-poli-ar/cmc/cmc-0292-ar.pdf>. accessed 09/09/2011

independence. In Qatar,⁸¹⁴ the Central Bank only restricts SSB members from receiving credit facilities for commercial use, but not for personal use. If the regulator is using such controls to enhance Shari‘ah supervisors’ independence, the prohibition ought to be extended to credit facilities for both personal and commercial purposes.⁸¹⁵

5.4.5.4. Ownership of Shares in IIFS

In contemporary Islamic finance literature, SSB members are sometimes compared to external auditors. However, while the latter’s financial investment in the audited entity is strictly prohibited and is seen as a threat to auditor’s independence,⁸¹⁶ not all Shari‘ah scholars see SSB’s investment from the same perspective.⁸¹⁷ Some scholars believe that it is religiously permissible for SSB members to own a small share in the institution (for example, less than 5%) if it is permissible by law. Such a percentage is not considered a large enough investment to endanger the independence of the SSB’s judgment.⁸¹⁸ Moreover, it is argued that members should not be prevented from investing in an entity, as they are more aware than anyone else of its level of compliance. Shari‘ah scholars’ piety and ethical standards should avert the effect of any conflict of interest.⁸¹⁹ However, others argue that since an SSB report is a testimony which certifies the compliance of IIFS, its members should be banned

⁸¹⁴ Qatar Central Bank (QCB), "Instructions to Banks," Qatar Central Bank, Eleventh Edition, March, http://www.qcb.gov.qa/English/Legislation/Documents/instructionsMar09_Eng/SEVEN.pdf. accessed 29 April 2011

⁸¹⁵ Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK," p100.

⁸¹⁶ See: Strohm, *United States and European Union Auditor Independence Regulation: Implications for Regulators and Auditing Practice*, p18.

⁸¹⁷ al-Ṣāliḥ, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maṣārif al-Islāmiyyah " p17; Yūsuf ‘AbdAllāh al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif: Ḍawābiḥā Wa Aḥkāmḥā Wa Dawrhā fī Ḍabṭ ‘Amal al-Maṣārif" (ibid.), p10.

⁸¹⁸ Muḥammad Aḥmad al-Ṣāliḥ, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maṣārif al-Islāmiyyah " (ibid.), p17; Yūsuf ‘AbdAllāh al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif: Ḍawābiḥā Wa Aḥkāmḥā Wa Dawrhā fī Ḍabṭ ‘Amal al-Maṣārif" (ibid.), p10.

⁸¹⁹ Qaṭṭān, "al-Raqābah al-Shar‘iyyah al-Fa‘ālah Fī al-Maṣārif al-Islāmiyyah " p21.

from any action which may call its credibility into question.⁸²⁰ The decision of the International Islamic Fiqh Academy is in favour of the latter restriction.⁸²¹ Nevertheless, regulations are generally silent on this matter. This might be because of the unclear role and legal status of SSB members, which this chapter has already discussed.

5.4.5.5. Working in an Executive Position

A Shari'ah supervisor's independence can be compromised if he takes on an executive role in the IIFS, since working in such a post may require him to take a supportive view of management's actions and decisions. For instance, the Dubai Islamic Bank (DIB), one of the largest Islamic financial institutions in the United Arab Emirates, has an SSB which serves as an external Shari'ah auditor, as well as an internal Shari'ah unit, which acts as an internal auditor. The issue is that the same scholar, Hussain Hamed Hassan, chairs both the DIB's external SSB and the internal Shari'ah unit based at the bank.⁸²² Moreover, Mohamed Abdulhakim Zoeir, who is a member of the SSB and its secretary, has also been appointed by the board of directors as an internal Shari'ah auditor.⁸²³ In this situation, there is a potential conflict of interest, since two of the SSB members work as an external auditor and employee on the payroll of the bank. Surprisingly, when this issue was raised before

⁸²⁰ Ahmad 'AbdAllāh Ibn Ḥumayd, "Dawr al-Raqābah al-Shar'iyyah Fī Ḍabṭ a'māl al-Maṣārif al-Islāmiyyah" (paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/9/2009), p6; Yūsuf 'AbdAllāh al-Shabīlī, "al-Raqābah al-Shar'iyyah 'Alā al-Maṣārif: Ḍawābiṭhā Wa Aḥkāmhā Wa Dawrhā fī Ḍabṭ 'Amal al-Maṣārif" (ibid.26/4/2009), p10; 'Abd āl-Ḥamid al-Ba'ī, "Astiql-āliyyat al-Hay'ah al-Shar'iyyah Fī al-Mu'assasāt al-Māliyyah al-Islāmiyyah " (paper presented at the The 2nd Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 29-30/10/2002), p30.

⁸²¹ al-'Yāashyī al-Ṣādiq Fidād, "Ta'arūḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'iyyah " (paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 18-19/5/2009), p16-17.

⁸²² Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p93.

⁸²³ Dubai Islamic Bank (DIB), "Hay'ah al-Fatwā Wa al-Raqābah al-Shar'iyyah " DIB,, <http://www.dib.ae/ar/shariaboard.htm>. accessed 29 April 2011; al-Islāmbūlī, "Dawr al-Hay'āt al-Shar'iyyah Fī Ḍabṭ A'māl al-Mu'assasāt al-Māliyyah al-Islāmiyyah " p23.

the head of DIB's Shari'ah Coordination Department, he argued that it presented no threat to SSB members' independence, since they are protected by the general assembly of shareholders.⁸²⁴ It does not seem to be a matter for concern that the head of the external SSB is at the same time the head of the body which oversees the implementation of SSB decisions. Nevertheless, Qatar Financial Centre rules clearly prohibit the appointing of SSB members in executive positions.⁸²⁵ This is also the position adopted by the Financial Conduct Authority, as can be indirectly understood from its standard for directors known as the "Fit and Proper Test for Approved Persons".⁸²⁶

Considering these five roadblocks to SSB independence, scholars have made a couple of recommendations to enhance SSB autonomy. One suggestion by Grais and Pellegrini⁸²⁷ is to apply a mandatory rotation for SSBs. It has been argued that an enduring relationship between the Shari'ah board and IIFS management can weaken the objectivity of its auditing. Thus, if a mandatory rotation were imposed to intercept such a relationship, the IIFS executive would not have the leverage of terminating SSB tenure to influence its decisions. However, apart from its cost,⁸²⁸ Summer argues that application of such a measure to external auditors would undercut inducements to

⁸²⁴ Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p94.

⁸²⁵ Qatar Financial Centre Regulatory Authority (QFC), "Islamic Finance Rulebook (ISFI)," Qatar Financial Centre (QFC), http://www.complinet.com/net_file_store/new_rulebooks/q/f/QFCRA_1935.pdf. accessed 29 April 2011; Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p101.

⁸²⁶ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*, p13-14. See also, Financial Conduct Authority (FCA), "What is an approved person?"; "The Fit and Proper test for Approved Persons".

⁸²⁷ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁸²⁸ Miles B. Gietzmann and Pradyot K. Sen, "Improving Auditor Independence Through Selective Mandatory Rotation," *International Journal of Auditing* 6, no. 2 (2002).

develop a reputation for integrity.⁸²⁹ Moreover, it might result in insufficient reviewing of Shari‘ah compliance during the transitional period, and it might also cause inconsistent implementation of Islamic finance within the same institution. To overcome the last two criticisms, Grais and Pellegrini⁸³⁰ suggest a partial compulsory rotation of SSB members rather than of the whole board. Such a solution would ensure greater independence for Shari‘ah supervisors and maintain the quality of Shari‘ah auditing as the remaining members would assure consistency in board resolutions.

Clarifying the SSB’s role in the IIFS articles of association can also help to improve SSB autonomy. These articles should include provisions that clearly state the need for SSB independence and its power to access records and information required to ensure Shari‘ah compliance. In addition, they should state the Shari‘ah board’s position in the institutional structure and the IIFS policy for appointing, dismissing, and fixing remuneration of SSB members.⁸³¹

In terms of fiscal autonomy, it has been suggested that SSBs should have their own independent budget approved by shareholders at the AGM. It should be sufficient to meet the SSB’s needs for research, software, and expertise. SSBs should be able to spend their budget without the interference of the IIFS board of directors and management.⁸³²

Admittedly, some of the suggested solutions are not always applicable—for example, where the IIFS operates within a secular environment or where regulators have a passive attitude towards Islamic finance. In this case, shareholders ought to

⁸²⁹ Martin Summer, "Does Mandatory Rotation Enhance Auditor Independence," *Zeitschrift für Wirtschafts- und Sozialwissenschaften* 118, no. 3 (1998). cited in Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁸³⁰ "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁸³¹ Ibid.; al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p28-31.

⁸³² Ibn Ḥumayd, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maṣārif al-Islāmiyyah," p7.

modify IIFS articles of association to enhance SSB independence, as this might be the only legally enforceable solution.

Regulators as well as IIFS ought to play a proactive role in ensuring the autonomy of SSBs.⁸³³ First, they should assert SSB independence in their rules and guidelines, as is the case in Kuwait's regulation of IIFS.⁸³⁴ Second, they should task the IIFS management with ensuring Shari'ah board independence and preventing any conflict of interest. The Qatar Financial Centre, for example, currently takes such measures.⁸³⁵ Third, to avoid the influence of a few individuals during the SSB's appointment in the AGM, IIFS should submit SSB candidates to a regulatory body for final approval, as do regulators in Malaysia, UAE, and Syria.⁸³⁶

A vital question for regulators is whether SSBs should be subject to the same strict independence requirements as auditors or independent directors are.⁸³⁷ SSB members are not outsiders, like auditors who are only concerned with *ex post* auditing. Neither are they part of the board of directors, like non-executive directors. There have not been any reports of a crisis due to a lack of SSB independence and conflicts of interest. However, the Islamic finance market is relatively new. Regulators should learn from auditing industry crises and start acting before scandals such as those faced

⁸³³ Notably, although the Islamic financial market in Syria is relatively new, regulators have addressed a lot of independent threats in this section. See: Monetary and Credit Council [MCC], "Admission Rules of SSB of Islamic Banks Operating in The Syrian Arab Republic 404, MN, B4".

⁸³⁴ 'Abd āl-Ḥamid al-Ba'ī, "al-Qawānīn Wa al-Tashrī'āt al-Maṣrifīyyah al-Islāmiyyah Dirāsāt Muqāranah " (paper presented at the The 7th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 27/5/2008), p58.

⁸³⁵ Qatar Financial Centre Regulatory Authority (QFC), "Islamic Finance Rulebook (ISFI)" p13 section 6.1.5.

⁸³⁶ al-Khalīfī, "al-Nazariyyah al-'Āmmah Lil-hay'āt al-Shar'iyyah " p33; Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p79; al-Ṣalāhīn, "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyyah Wa Dawruhā Fī al-Maṣrifīyyah al-Islāmiyyah " p258-59; Qattān, "Hay'ah al-Raqābah al-Shar'iyyah Akhtiyār A'ḍā'ihā Wa Dawābiṭhā "; Monetary and Credit Council [MCC], "Admission Rules of SSB of Islamic Banks Operating in The Syrian Arab Republic 404, MN, B4" Art 3-5.

⁸³⁷ On non-executive directors' independence, see: Mallin, *Corporate Governance*, p174-75.

by Enron, Tyco International, and WorldCom⁸³⁸ occur. It is true that SSB members are generally well-regarded Shari'ah intellectuals with a high ethical standard.⁸³⁹ Nevertheless, they are human and they are not infallible. If Islamic finance leaders are serious about competing on a global level, they should note that the local reputation of a scholar's integrity may not be sufficient to allay market suspicions over SSB conflicts of interest and lack of independence.

5.4.6. Conflicts of Interest

The growth of the Islamic financial industry has outstripped the number of qualified Shari'ah supervisors,⁸⁴⁰ resulting in the same Shari'ah scholar holding appointments at many different institutions.⁸⁴¹ A 2011 study conducted by Ünal⁸⁴² shows that the top 20 Shari'ah scholars each sit on 14 to 85 board positions in the Islamic finance industry. The top 10 Shari'ah scholars hold 450 SSB positions, which represent 39.44% of available positions in the world. Table 3 lists the top 10 SSB members worldwide. The second column shows the total number of board positions which each scholar holds in Islamic finance institutions. The third column represents the total number of positions that each scholar holds, including their membership in financial institutions, standard-setting organisations, national regulatory bodies, foundations, unions, and Shari'ah consulting firms.

⁸³⁸ See generally about Enron, Tyco International, and other crises: Thomas Clarke, *International Corporate Governance: a Comparative Approach* (London: Routledge, 2007), p14-16.

⁸³⁹ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". *Fidāh*, "Ta'āruḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'iyyah " p11. It is worth pointing out that 75% of the respondents in a study conducted in Malaysia in 2009, believe that the independence of the SSB is not affected by remuneration. The fact that Shari'ah supervisors are generally full-time academics could be the reason for such findings: See Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* p48.

⁸⁴⁰ Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p92.

⁸⁴¹ Siti Faridah Abd Jabbar, "International - The Shari'a Supervisory Board: a Potential Problem in Islamic Finance," *The Company lawyer* 29, no. 1 (2008): p30.

⁸⁴² Murat Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective," *Funds@Work*, http://www.funds-at-work.com/fileadmin/downloads/Sharia-Network_by_Funds_at_Work_AG.pdf.pdf. accessed 5 February 2011

Table 3. Top 10 SSB Members Worldwide

| Scholar name | Positions in IFIs | Overall positions |
|-----------------------------|-------------------|-------------------|
| Abdul Satar Abu Ghuddah | 85 | 101 |
| Nizam Yaquby | 85 | 95 |
| Mohammed Eid Elgari | 71 | 86 |
| Abdulaziz Khalifa Al-Qassar | 39 | 41 |
| Abdulla Sulaiman Al Manea | 36 | 42 |
| Hussein Hamid Hassan | 31 | 39 |
| Mohamed Daud Bakar | 27 | 43 |
| Essa Zaki Essa | 27 | 27 |
| Ali Al Qaradaghi | 25 | 35 |
| Ajeel Jassim Al Nashmi | 24 | 27 |

Source: Ünal (2011)

Although membership on multiple boards can give SSB members greater independence than they would have if serving just one institution, it raises concerns about breaching the confidentiality of IIFS. This risk arises because the role of SSBs is to ensure Shari‘ah compliance of a financial institution, so its members have access to all institutional records and sensitive information. To mitigate the risk of accidental or deliberate leaks of confidential information, IIFS management might try to conceal information from the SSB, which would affect the process of securing Shari‘ah compliance in the institution.⁸⁴³

The potential abuse of sensitive information is a second concern related to SSB conflicts of interest. Because IIFS directors often discuss the details of any potential deals or investments to ensure their Shari‘ah compliance prior to their disclosure in the market, SSB members could theoretically use that information to their personal

⁸⁴³ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

financial advantage, especially when no regulations prevent SSB members and their relatives from investing in the company.⁸⁴⁴

A third issue that results from multiple SSB membership is the creation of a “*fatwa* shopping” phenomenon, where SSB members are hand-picked for their ability to provide a *fatwa* that suits the financial institution, regardless of its conflict with the spirit of Islamic law. The more lenient a Shari‘ah scholar is, the more his name appears on SSBs and the more he is sought after in the industry.⁸⁴⁵ This has led some Shari‘ah scholars to compete on the basis of their leniency, not on the quality of their supervision.

Multiple membership in SSBs raises a fourth problem of granting a small group of people a considerable amount of power over the direction of the industry. As mentioned, Ünal’s 2011 study of SSB networks showed that almost 40% of Shari‘ah board positions in the world are held by the top 10 scholars; moreover, the top 100 scholars sit on nearly 84% of the SSBs around the globe.⁸⁴⁶ This concentration of power is potentially very dangerous, since it places the future of the industry in the hands of an international Shari‘ah cartel.⁸⁴⁷ This situation may hinder the industry’s jurisprudential growth by closing the door for junior scholars to join the industry.

A fifth concern is that membership on multiple SSBs can create a Shari‘ah compliance risk. Multiple membership places a Shari‘ah scholar under great pressure from different institutions to review contracts and sign off on documents. To cope

⁸⁴⁴ Abd Jabbar, "The Sharia Supervisory Board of Islamic Financial Institutions: A Case for Governance," p244; Fidād, "Ta‘arūḍ al-Maṣāliḥ Fī A‘māl Hay’āt al-Riqābah al-Shar‘iyyah " p17; Mūsā Ādam ‘īsā, "Ta‘arūḍ al-Maṣāliḥ Fī A‘māl Hay’āt al-Riqābah al-Shar‘iyyah" (paper presented at the The 8th Conference of Shari‘a Supervisory Boards of Islamic Financial Institutions, Bahrain, 18/5/2009), p25.

⁸⁴⁵ Abdulbari Mashal, "Dawr al-Ma‘āyir al-Shar‘iyyah Wa al-Muḥāsabiyyah Fī Tanzīm al-Maṣrifīyyah al-Islāmiyyah " (paper presented at the The 2nd Conference of Islamic Financial Services, Tripoli-Libya, 27-28/4/2010), p7.

⁸⁴⁶ Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

⁸⁴⁷ Wright, "The Shariah Scholar Cartel".

with such tasks, SSB members spend less time ensuring Shari‘ah compliance so that they can deliver their approval quickly.⁸⁴⁸ This raises concerns over the quality of Shari‘ah auditing and can lead to huge liability for the audited entity and its investors. Lahem Al-Nasser,⁸⁴⁹ an expert in Islamic finance and the head of an Islamic banking advisory institution, questions the ability of SSB members with numerous board memberships in different countries to provide adequate Shari‘ah review, given the complexity of financial instruments and the amount of time usually spent in SSB meetings. In fact, the duration of an SSB meeting is not sufficient to read the documents presented, let alone to carefully check and understand all the details and structure of a proposed product. He recalls an incident where an SSB member approved 72 *sukūks* (Islamic bonds) in a single meeting, notwithstanding their complexity and controversial validity in the industry.⁸⁵⁰ Another researcher reports that some SSB scholars rely on the approval of other members of the board when ratifying products, rather than making an independent judgment.⁸⁵¹

Multiple membership on SSBs further jeopardizes Shari‘ah compliance because famous SSB members serve on numerous boards in different countries where various schools of thoughts are followed. SSB members sometimes dispute the religious permissibility of a product, and since decisions are made by a majority vote, Shari‘ah scholars might end up with conflicting views prohibiting a product on one board and approving it on another.⁸⁵² This inconsistency might confuse investors and shake their trust in the scholar.⁸⁵³

⁸⁴⁸ Siddiqui, "A Sharia Scholar's Place on The Board"; Howladar, "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance".

⁸⁴⁹ al-Nasser, "Waḍ' al-Maṣrifīyah al-Islāmiyyah Murbik Wa Naḥn Biḥājah ilā Wilādah Jadīdah ".

⁸⁵⁰ Ibid.

⁸⁵¹ Zighībah "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Ḥulūl Muqtarahah " p27.

⁸⁵² Qaṭṭān, "al-Raqābah al-Shar'īyyah al-Fa'ālah Fī al-Maṣārīf al-Islāmiyyah " p15.

⁸⁵³ Ibid.

In the face of these criticisms, a few justifications have been offered for multiple memberships on SSBs. The Islamic finance literature has long cited the shortage of Shari‘ah scholars when rationalising multiple memberships.⁸⁵⁴ However, it is questionable whether there is a real lack of qualified scholars, or whether that is mainly an excuse for financial institutions to appoint certain SSB members. Zulkifli Hasan⁸⁵⁵ suggests that this supposed shortage is simply a myth, noting that despite the establishment of modern Islamic finance more than 30 years ago and the organisation of hundreds of conferences, workshops, and seminars, the same excuse is being used. He argues that there are numerous qualified Shari‘ah scholars who could be employed in the industry.⁸⁵⁶ Professor Mohammad Akram Laldin,⁸⁵⁷ a renowned SSB member and the director of the International Shari‘ah Research Academy for Islamic Finance (ISRA), shares the same firm belief that the market does not lack for Shari‘ah supervisors. Rather, Laldin contends that there is a sufficient number of proficient scholars for SSBs, but the industry has not given them the opportunity to sit on SSBs.⁸⁵⁸

The claim of a shortage of Shari‘ah scholars is further discredited by the existence of many higher academic institutions which offer specialised education in Islamic law. These institutions are spread across the world, and thousands of students graduate from them every year. Saudi Arabia, for example, has nine universities with a special college for Shari‘ah law and Islamic studies.⁸⁵⁹ Egypt has the renowned Al Azhar University, where around 1,500 students graduate with a BA from Shari‘ah

⁸⁵⁴ Zulkifli Hasan, "Demystifying The Myth Of Shortage Of Shari'ah Scholars", *Global Islamic Finance Magazine*. accessed

⁸⁵⁵ Ibid.

⁸⁵⁶ Ibid.

⁸⁵⁷ Ibid.

⁸⁵⁸ Ibid.

⁸⁵⁹ Khālid al-Mashūh, "Taṭwīr Kuliyyāt al-Sharī‘ah " Alwatan, <http://www.alwatan.com.sa/Articles/Detail.aspx?ArticleId=2887>. accessed 10 July 2011

colleges every year, along with 300 Masters graduates and 30 PhDs.⁸⁶⁰ In Malaysia, there is the International Centre for Education in Islamic Finance (INCEIF), which along with other top universities in Syria, Jordan, UAE, Kuwait, Qatar, Morocco, Algeria, Pakistan, India, and Indonesia offers special courses in Islamic jurisprudence.⁸⁶¹ Accordingly, it seems safe to assume that there are many underutilised Shari'ah specialists who could meet the demands of the Islamic finance industry.

However, this assumption might not be completely accurate, as not all Shari'ah graduates may be able to function properly on an SSB. In the words of one of the top 10 SSB members, Hussain Hamid Hassan, "Graduating from a Shari'ah college is not enough by itself".⁸⁶² This is because the standard curriculum in these academic institutions is not directed at producing professionals in Islamic finance, but rather general specialists in Shari'ah law, of which Islamic finance is one complex part. Moreover, classes on Islamic finance often focus on the simple structures found in classical jurisprudence, creating a disconnection between the curricula taught in these universities and the financial instruments and vehicles used in the market.⁸⁶³ In short, a Shari'ah graduate may not necessarily be able to assess whether or not a particular financial product is Shari'ah compliant, because issuing such a judgment requires not only knowledge of Islamic jurisprudence, but also an understanding of the actual implementation of the product in the financial industry.

Nevertheless, this situation does not justify the domination of SSBs by just a few scholars. The majority of the top SSB members were full-time academics at one point,

⁸⁶⁰ Khorshid, "Shariah Board Accountability".

⁸⁶¹ Hasan, "Demystifying The Myth Of Shortage Of Shari'ah Scholars."

⁸⁶² Siddiqui, "A Sharia Scholar's Place on The Board".

⁸⁶³ Quṭb al-Rīsūnī, "Naḥw Ta'hīl Ajtihādī Li'A'dā' Hay'ah al-Fatwā bi-al-Maṣārifī al-Islāmiyyah" (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5 - 3/6/2009), p16-17.

and some still are. They share the responsibility with the industry for not partnering with academic institutions to teach the next generation of SSB members. In addition, Shari‘ah graduates’ lack of competence in this domain could be overcome in the short term through intensive courses and training programmes. In the long term, the focus should be on improving the quality of the education offered in Shari‘ah colleges to meet the needs of the modern Islamic finance industry. Malaysia has taken the initiative in this area by allocating the sum of 700 million ringgits for three established trusts devoted to Islamic finance education and training.⁸⁶⁴ These trusts include INCEIF, with a fund of 500 million ringgits, and ISRA, which was allocated 100 million ringgits. 100 million ringgits were also provided to the Malaysia Central Bank Shari‘ah Development Fund, which is intended to increase the number of qualified Shari‘ah scholars and is open to citizens of all countries.⁸⁶⁵

In this regard, it is worth pointing out the different attitudes of Malaysian SSB members towards regulation and reform, compared with their peers in the GCC countries.⁸⁶⁶ While the former acknowledge some of the issues arising from multiple SSB membership and have supported a governance reform, top SSB members in the Gulf seem to deny the existence of a real conflict of interests,⁸⁶⁷ and they firmly disagree with the idea of restricting Shari‘ah scholars to one supervisory board. They further justify the multiplicity of SSB memberships by comparing themselves to

⁸⁶⁴ Mushtak Parker, "Islamic Banking Special Supplement: Shariah Governance a Challenge to Islamic Banking," Arab News, <http://archive.arabnews.com/?page=9§ion=0&article=127292&d=11&m=10&y=2009>. accessed 15 October 2010; Bank Negara Malaysia (BNM), "Shariah Scholarship Award," Bank Negara Malaysia, <http://www.bnm.gov.my/index.php?ch=200&pg=618&ac=529>. accessed 20 May 2011

⁸⁶⁵ Parker, "Islamic Banking Special Supplement: Shariah Governance a Challenge to Islamic Banking"; Bank Negara Malaysia (BNM), "Shariah Scholarship Award".

⁸⁶⁶ This is the position of top SSB members in the Islamic finance industry, like Nizam Yaquby, Mohamed Al Qari, and Hussain Hamid Hassan. Needless to say, there are some GGC scholars who have called for limiting SSB membership numbers and agree with the Malaysian approach.

⁸⁶⁷ It is interesting to see that Al Qari rejects concerns over conflicts of interest but in the same interview recalls an incident where he was advising two banks which were separately developing versions of the same product for nine months. See Wright, "The Shariah Scholar Cartel".

lawyers and accountants,⁸⁶⁸ notwithstanding the fact that SSB members do not adhere to a code of practise similar to that which governs these two professions.

Popular SSB members further justify their multiple memberships by presenting themselves as lifesavers of the Islamic finance industry, citing as pretexts their experience and the exaggerated risk of handing SSBs over to young scholars.⁸⁶⁹ In fact, one top SSB member goes as far as faulting those who believe that Shari'ah graduates from an appropriate educational background, given current curricula, could meet the demands of the industry.⁸⁷⁰ These behaviours call into question the credibility of claims that there is a shortage of Shari'ah scholars and suggest that the real issues are rather those of bad governance practises and the old guard trying to protect their private interests.

Perhaps the first solution that comes to mind when addressing the issue of conflicts of interest is to limit the number of SSB positions a Shari'ah scholar can hold, as regulators in Malaysia and Pakistan already do. However, although this measure could overcome concerns about confidentiality, it could also preclude the creation of a professional market for Shari'ah auditors by reducing the financial attraction towards the profession. Moreover, it could build a mutually beneficial relationship between SSB members and the audited entity, thus affecting auditor independence.⁸⁷¹ Nonetheless, restricting the number of Shari'ah supervisory positions per individual would facilitate the appointment of a new generation of Shari'ah scholars and combat the domination of SSB membership. In a country where

⁸⁶⁸ Frederik Richter, "Top Islamic Finance Scholars Oppose Reform Effort," Reuters, <http://www.reuters.com/article/2010/12/01/islamicfinance-scholars-idUSLDE6B015920101201>, accessed 3 December 2010; Siddiqui, "A Sharia Scholar's Place on The Board"; Wright, "The Shariah Scholar Cartel"; El Baltaji and Anwar, "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance".

⁸⁶⁹ Khorshid, "Shariah Board Accountability"; Siddiqui, "A Sharia Scholar's Place on The Board".

⁸⁷⁰ Wright, "The Shariah Scholar Cartel"; El Baltaji and Anwar, "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance".

⁸⁷¹ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

there is a real shortage of Shari‘ah scholars, regulators could deal with the numbers involved in board membership on a case-by-case basis, according to the performance of the individual applicant, the category of the financial institution they are involved with, and the status of the scholar within the board (chairman vs. member).

However, focusing on board membership numbers would not give regulators the full picture.⁸⁷² Regulators should consider various factors when addressing this issue, for instance, the size of the financial institution where a scholar sits on the SSB, the category of the financial work (banking or insurance),⁸⁷³ the scholar’s standing within the SSB (chairman or member), and the ease of the scholar’s access to other powerful scholars in the industry, which can affect their perspective and influence. This last point can be illustrated with the case of Mohamed Ali Al-Tashkeri; although he generally only holds four positions, he is ranked as number 15 in terms of his ability to quickly access highly ranked SSB members in the industry. Another example is Ahmad Ali Abdulla, who is ranked as number 36 in terms of total board membership, but as number 19 when taking into account his close connection with other powerful Shari‘ah scholars in the industry who share board membership with him.⁸⁷⁴

To fully understand the potential conflicts of interest facing an SSB member, regulators should also pay attention to his presence in standard-setting organisations, as well as in national and international regulatory bodies, and how this affects his membership on Shari‘ah supervisory boards in IIFS. For instance, Ünal’s 2011 study showed that the 12 most active scholars in the AAOIFI sit on 38.9% of the available

⁸⁷² Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

⁸⁷³ In Malaysia, an SSB member cannot be appointed as a member of another SSB in the same industry. The banking and *takaful* (Islamic insurance) industries are considered different industries. See: Bank Negara Malaysia (BNM), "Shari’ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p20.

⁸⁷⁴ Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

boards in Islamic finance institutions. Moreover, they collectively hold 71.17% of the positions in standard-setting organisations, governmental units and consulting companies.⁸⁷⁵ This domination raises a serious concern about regulatory independence⁸⁷⁶: how can we be assured that standards and frameworks introduced by these entities follow public interests and are not affected by regulatory capture?⁸⁷⁷ Accordingly, it is no wonder that the AAOIFI has so far failed to clearly address this issue and that its scholars have always objected to strict governance reforms.⁸⁷⁸

Another possible remedy for conflicts of interest is to issue a professional code of conduct for Shari'ah supervisors.⁸⁷⁹ Such guidelines should adequately address the way in which SSB members act when faced with a conflict of interest. The AAOIFI code of ethics for accountants and auditors of IFIs ignores this issue and instead directs its attention to general Islamic ethics, quoting Shari'ah provisions, which makes it difficult to enforce in secular countries. In this case, regulators may extend the code for external auditors to include Shari'ah supervisors.⁸⁸⁰ Nevertheless, the code should be overseen by a regulatory body and incorporate penalties for the violation of its duties. SSBs could then refer to this body with any concerns over conflict of duties.⁸⁸¹

Finally, investing in contemporary Islamic finance education and incentive training programmes for potential SSB members should pay off and reduce the

⁸⁷⁵ Ibid.

⁸⁷⁶ Alsayyed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance".

⁸⁷⁷ Regulatory capture occurs when a regulatory body, created to protect the public's interest, ultimately takes an action benefitting the industry which it is assumed to be regulating, rather than the public. See: Ernesto Dal Bó, "Regulatory Capture: A Review," *Oxford Review of Economic Policy* 22, no. 2 (2006).

⁸⁷⁸ See: Richter, "Top Islamic Finance Scholars Oppose Reform Effort".

⁸⁷⁹ Fidād, "Ta'arūḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'iyyah " p17; 'Isā, "Ta'arūḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'iyyah," p22-23.

⁸⁸⁰ Graiss and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

⁸⁸¹ 'Abd al-Sattār 'Alī al-Qaṭṭān "Madā Ta'arūḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'iyyah" (paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 18-19/5/2009), p12-13.

demand on “superstar” SSB members. Malaysia has the lead in this regard, with many academic institutions and funds dedicated to promoting Islamic finance. These include the INCEIF, Bank Negara, Shari‘ah Research Grants, and the Association for Islamic Finance Advancement (AIFA).⁸⁸² By 2020, Malaysia aims to attract 55,000 local and 28,000 international students to its Islamic finance courses.⁸⁸³ In the UK, the Islamic Finance Council UK, in association with the Securities and Investment Institute and Islamic Banking and Islamic Insurance, has introduced special courses designed to train a potential Shari‘ah supervisor.⁸⁸⁴ In addition, the universities of Durham, Reading, and Bangor are amongst those academic institutions offering postgraduate courses in Islamic finance across the UK.⁸⁸⁵

5.4.7. *Lack of Competence*

SSB work has a religious nature, as its decision is regarded as *fatwa* (religious legal opinion). Therefore, its members must fulfil the ethical, educational, and technical requirements of qualified Shari‘ah scholars. As far as ethics are concerned, apart from being Muslim, scholars must meet the requirements of ‘*adālah* (upright character).⁸⁸⁶ This includes uprightness in religion, honesty, truthfulness, and good manners.⁸⁸⁷

⁸⁸² Bank Negara Malaysia (BNM), "Shariah Scholarship Award"; The International Centre for Education in Islamic Finance (INCEIF), INCEIF,, <http://www.inceif.org/home/papers>. accessed 30 May 2011; The Association for Islamic Finance Advancement (AIFA), AIFA,, <http://aifa-i.org/>. accessed 30 May 2011

⁸⁸³ Emmy Abdul Alim, "Malaysia Seeks to be Global Educational Hub," The Islamic Globe, http://www.theislamicglobe.com/index.php?option=com_content&view=article&id=282:malaysia-seeks-to-be-global-educational-hub&catid=17:survey&Itemid=74. accessed 23 May 2011

⁸⁸⁴ The Islamic Finance Council UK (IFC), IFC,, <http://www.islamicfinancecounciluk.com/>. accessed 23 May 2011; Institute of Islamic Banking and Islamic Insurance(IIBI), "About Us," IIBI,, <http://www.islamic-banking.com/about.aspx>. accessed 23 May 2011; Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK."

⁸⁸⁵ Harriet Swain, "Islamic Finance Gives Universities a Bonus", *The Guardian*, 28 July 2009 <http://www.guardian.co.uk/education/2009/jul/28/business-schools-islamic-finance>. accessed 23 May 2011

⁸⁸⁶ Kamali, *Principles of Islamic Jurisprudence*, p468.

⁸⁸⁷ al-Khalīfī, "al-Nazariyyah al-‘Āmmah Lil-hay’āt al-Shar‘iyyah " p85-62; al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif:Ḍawābiḥā Wa Aḥkāmā Wa Dawrhā fī Ḍabṭ ‘Amal al-Maṣārif," p15-18.

From the scholarly point of view, an SSB member must be classified as *mujtahd*, which includes being very well versed in Shari‘ah in general, with particular expertise in Islamic commercial law. He should be fluent in classical Arabic to be able to deal directly with Shari‘ah sources. He should also have a sufficient understanding of *uṣūl al-fiqh* (the principles of Islamic jurisprudence), *maqāṣid al-sharī‘ah* (the objectives of Islamic law), and *al-siyāsah al-shar‘iyyah* (Shari‘ah-based policy or politics).⁸⁸⁸

From a technical perspective, scholars must be familiar with modern banking, business, and legal practises.⁸⁸⁹ This is crucial to avoiding any disconnection between the theoretical concepts of Islamic finance and its implementation in the market. A recent survey of Shari‘ah advisors, Shari‘ah bank officers, and regulators in Malaysia showed that 83% of respondents agreed on the necessity for legal expertise on SSBs. In addition, 63% of participants voiced fair support that business qualifications should be required from SSB members, while 17% firmly supported such a proposal.⁸⁹⁰

English proficiency is another vital skill for SSB members, because contracts, forms, and agreements are frequently in English. Since most SSB members are not fluent in English, a translated version is usually provided. However, a poor translation makes it difficult for scholars to understand the actual terms of the agreement, which consequently affects the soundness of their judgment.⁸⁹¹ Furthermore, communication skills and the ability to work on a team in a multi-disciplinary environment are

⁸⁸⁸ Fāris, "Ḍawābiṭ Wa Āliyyāt Akhtiyār A‘dā’ Hay’āt al-Fatwā Wa al-Riqābah al-Shar‘iyyah Fī al-Mu’asasāt al-Māliyyah " p13-20,p 40-41; DeLorenzo, "Shari‘ah Supervision in Modern Islamic Finance"; Qattān, "Hay’ah al-Raqābah al-Shar‘iyyah Akhtiyār A‘dā’ihā Wa Ḍawābiṭhā " p4-5.

⁸⁸⁹ Ghoul, "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products," p90; Khālid al-Muzaynī, "Tarshīd al-‘Amal Fī al-Ha’āt al-Shar‘iyyah Lil-mu’assasāti al-Māliyyah al-Islāmiyyah" (paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5 - 3/6/2009), p12; Ahmad al-Duwayhī, "Ḍawābiṭ al-Ijtihād fī al-Mu’āmalāt al-Māliyyat al-Islāmiyyah" (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, Dubai, UAE, 15-17/5/2005), p91.

⁸⁹⁰ Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p46.

⁸⁹¹ Ibn Ḥumayd, "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maṣārif al-Islāmiyyah," p9; Qattān, "Hay’ah al-Raqābah al-Shar‘iyyah Akhtiyār A‘dā’ihā Wa Ḍawābiṭhā " p18.

essential for SSB members, particularly when working with different departments in financial institutions to develop new products.⁸⁹²

In practise, an ideal scholar of this sort is very hard to find; few Shari‘ah scholars meet all of these requirements, particularly in the technical realm. Most SSB members lack financial, economic, and legal backgrounds, which hinders their ability to express a sound Shari‘ah view on complex modern financial practises.⁸⁹³

Perspective is another issue affecting SSB members’ competence. Shari‘ah scholars and bankers see from different standpoints.⁸⁹⁴ While the former focus on the Shari‘ah compliance of contracts, the latter aim to maximise profit in the most efficient way. This difference in mindset has resulted in Shari‘ah scholars proposing inefficient structures for contracts and products, thus creating a serious issue for financial institutions operating in a competitive environment.

Furthermore, scholars’ limited exposure to international financial practise poses a Shari‘ah risk to financial institutions. This risk can occur when SSB members approve a product or contract before knowing its real implementation in the market, then revise their decision when they see the product implemented. For example, the renowned scholar ‘AbdAllāh Sulimān al-Mani‘ recanted his authorisation of *ṣukūk al-ijārah* issued by the Bahraini government when he learned that possession of the underlying assets was not entirely conveyed to the lessor in the manner stated in *ijārah* (leasing) contracts in Islamic commercial law.⁸⁹⁵ Such incidents can profoundly damage the reputation and financial position of the institution. A number of financial

⁸⁹² DeLorenzo, "Shari‘ah Supervision in Modern Islamic Finance" p401; Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p56-57.

⁸⁹³ Bakar, "The Shari‘a Supervisory Board and Issues of Shari‘a Rulings and their Harmonisation in Islamic Banking and Finance," p78; Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p79.

⁸⁹⁴ Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p4-5.

⁸⁹⁵ El-Gamal, *Islamic Finance : Law, Economics, and Practice*, p23.

institutions have exacerbated this problem by taking advantage of SSBs' financial and commercial naiveté, either by not revealing all the required information or by presenting it in a way that guarantees SSB approval despite the fact the presentation does not reflect the product's actual implementation in the market.⁸⁹⁶ This might help explain the inconsistent decisions of different SSBs in the industry concerning the same products.

The first step in resolving the competence issue would be to establish specific standards for professionals working in Shari'ah supervision. Currently, there are no standards or regulations, not even an IIFS article of association which stipulates detailed qualifications and technical experience for SSB members.⁸⁹⁷ AAOIFI and Malaysian standards, for example, do not require a specific degree or qualification to show that an individual has the expertise to do the job, but only require SSB members to be expert in *fiqh al-mu'āmalāt* (Islamic commercial law) or even Shari'ah law in general.⁸⁹⁸ This might be because, in the early days of modern Islamic finance, financial institutions did not select SSB members based on their qualification for the task, but rather according to their reputation, which incentivised people to buy the IFI's products.⁸⁹⁹

Seeking the final approval of central banks in Malaysia and Pakistan before appointing SSB members might reduce the risk of recruiting unqualified people.

⁸⁹⁶ Abd Jabbar, "The Governance of Shari'a Advisers of Islamic Financial Institutions: The Practice in Malaysia," p313; Zighībah "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'iyyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Ḥulūl Muqtarahah " p24.

⁸⁹⁷ 'Umar, "A'māl al-Hay'āt al-Shar'iyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " p12-13; Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p76-78; Hassan et al., *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* p7.

⁸⁹⁸ The Pakistani requirements seem to be more specific in this regard; see: Aznan Hasan, "Optimal Shari'ah Governance in Islamic Finance," BNM, http://www.bnm.gov.my/microsites/giff2007/pdf/frf/04_01.pdf, accessed 17 October 2010

⁸⁹⁹ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p76-78; 'Umar, "A'māl al-Hay'āt al-Shar'iyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " p12.

However, for Shari'ah supervision to be regarded as a serious profession, like being a lawyer or accountant, individuals who wish to work on SSBs should obtain precise educational and technical qualifications designed for the task, and a governing body should be enabled by regulators to licence qualified Shari'ah professionals to work in the industry.⁹⁰⁰

As an immediate solution to this issue, some IIFS have taken certain measures. In the Sudan, for example, the legal department in the Islamic Co-operative Development Bank joins the SSB in the process of structuring contracts.⁹⁰¹ Other financial institutions, such as the Agricultural Bank of Sudan, have appointed lawyers, accountants, and economists to their SSBs.⁹⁰² The AAOIFI standard allows the SSB appointment of one person who is not a specialist in Islamic commercial law. However, while some argue that such experts should be given full membership on the board to ensure their objectivity and independence during SSB deliberations,⁹⁰³ others have criticised the right of non-Shari'ah qualified scholars to vote on Shari'ah-related issues.⁹⁰⁴ In addition, members of cross-disciplinary SSBs might find it difficult to reconcile different perspectives, posing the risk of communication failure between board members.⁹⁰⁵

⁹⁰⁰ "A'māl al-Hay'āt al-Shar'iyyah Bayn al-Istishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " p12-13; Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". Regulators in Malaysia are in the process of setting up a professional body which will carry out a similar function. See: Khalid Qayum and Soraya Permatasari, "Shariah Experts Push for Certification of Islamic Scholars," Bloomberg <http://www.bloomberg.com/news/2010-08-31/shariah-experts-prepare-first-certification-of-scholars-islamic-finance.html>. accessed 15 October 2010

⁹⁰¹ The Higher Sharia Supervisory Board for Banks & Financial institutions (HSSB), *Nash'at Wataṭawwūr Wataqwīm Ha'āt al-Riqābah al-Shar'iyyah fī al-Jihāz al-Maṣrifī al-Sūdānī* 1ed. (Khartoum: Central Bank of Sudan, 2006), p23.

⁹⁰² Ibid., p29.

⁹⁰³ Bakar, "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance," p78.

⁹⁰⁴ al-Islāmbūlī, "Dawr al-Hay'āt al-Shar'iyyah Fī Dabṭ A'māl al-Mu'asasāt al-Māliyyah al-Islāmiyyah " p7; Hassan, "al-'Alāqah Bayn al-Hay'āt al-Shar'iyyah wa al-murāji'īn al-khārijīyyīn " p10-11.

⁹⁰⁵ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services".

A final related question is whether SSB selection is currently based merely on qualifications to fulfil the task or on additional considerations as well. A recent survey conducted in Malaysia showed that new SSB members are mostly appointed as a result of suggestions from present members of the board.⁹⁰⁶ This raises the question of whether regulators should play a role in ensuring a more objective method for recruiting new Shari‘ah scholars, taking steps to prevent SSBs from being dominated by a small circle of Shari‘ah supervisors.

5.5. Conclusion

This chapter has aimed to gauge the extent to which Shari‘ah supervisory board governance practises contribute to the issue of creative Shari‘ah compliance in the contemporary Islamic finance industry. In particular, seven issues have been identified as main factors responsible for reducing the level of Shari‘ah compliance in IIFS. These issues are the SSBs’ unclear functions and legal status, lack of accountability and transparency, and conflicts of interest and lack of independence, as well as the poor training and inadequate qualifications of SSB members.

The chapter has proposed several suggestions to confront these challenges. For one, Shari‘ah supervision should be recognised as an independent profession. Like lawyers and accountants, its members should act within a framework that defines their legal status, role, and responsibilities. In cases where an IIFS is operating within a jurisdiction which does not favour Islamic finance or where regulators are passive, SSB members can take a proactive role in regulating Shari‘ah governance by working across SSBs to standardise their own contracts with financial institutions

⁹⁰⁶ Hassan et al., *An Analysis of the Role and Competency of the Shari‘ah Committees (SCs) of Islamic Banks and Financial Service Providers* p50; Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

Emphasising accountability and transparency in SSBs should not be perceived as showing less respect to Shari‘ah scholars or doubting their credibility, but rather as dealing professionally with an essential group in the industry and adding a layer of protection to public interests. This is particularly important if IIFS are operating in a global market where the local reputation of Shari‘ah board members may not be sufficient to allay stockholders’ suspicions over their reliability or SSBs’ lack of accountability and transparency.

A vital point of this chapter is to stress that in order to maintain sound financial systems and investor confidence, regulators in Islamic and secular countries have to recognise the need for their involvement in regulating Shari‘ah governance in IIFS. In other words, a solid Islamic financial market cannot be established unless Shari‘ah governance is regulated. The next chapter further emphasises regulators’ role and suggests two public mechanisms to remedy the issue of creative Shari‘ah compliance: establishing central Shari‘ah supervisory boards and enforcing compulsory disclosure.

Chapter Six: Public Mechanisms to Remedy Creative Shari‘ah Compliance

6.1. Introduction

Previous chapters of this thesis have critically appraised justifications of creative Shari‘ah compliance practises in contemporary Islamic finance and examined how Shari‘ah supervisory board (SSB) governance practises and inconsistent *fatwas* contribute to this issue. Chapter five stressed the need for regulators to take a proactive approach towards Shari‘ah governance in the Islamic finance industry. This chapter suggests two public mechanisms that involve a national regulator in remedying the issue of creative Shari‘ah compliance: establishing central Shari‘ah supervisory boards (CSSBs) and enforcing compulsory disclosure.

The chapter is structured in nine parts including this introduction. Part 6.2 provides an overview of regulators’ approaches towards CSSBs and addresses the rationale for establishing these boards. Part 6.3 discuss the tasks of CSSBs. Part 6.4 and Part 6.5 examine CSSBs in Sudan and Malaysia, while Part 6.6 and Part 6.7 evaluate regulatory approaches in the United Kingdom and Saudi Arabia towards Shari‘ah governance and CSSBs. Part 6.8 suggests enforcing compulsory disclosure as a remedy for creative Shari‘ah compliance, and Part 6.9 concludes the chapter.

6.2. Overview and Justification of CSSBs

One of the main ways to remedy the issue of creative Shari‘ah compliance is to establish a central Shari‘ah Supervisory Board (CSSB) to oversee Shari‘ah governance and the practise of Islamic finance in the financial industry. Regulators in Islamic and secular countries have different attitudes towards Shari‘ah governance

and the importance of a CSSB. According to Zulkifli Hasan,⁹⁰⁷ the regulatory approaches followed by authorities in various jurisdictions can be divided into four categories:

1. **Passive approach**, where the regulatory authority does not intervene in regulating SSBs or play a role in ensuring Shari‘ah compliance. One entity that takes this approach is the Saudi Arabian Monetary Agency (SAMA), which has no specific regulations for Islamic finance. There is no CSSB, and the establishment of an SSB at individual institutions is a private matter and merely self-motivated.
2. **Reactive approach**, which is more prevalent in secular legal jurisdictions such as the UK and Turkey. Authorities in these countries have licensed the establishment of many institutions offering Islamic financial services (IIFS) and have amended tax regulations to accommodate some Shari‘ah-compliant products. There are no particular rules regulating IIFS, but they are obligated to conform to the established conventional legal framework. IIFS management bears responsibility for ensuring Shari‘ah compliance. The UK Financial Conduct Authority (FCA) plays no role with regard to Shari‘ah governance, but states that the status of SSBs should be merely an advisory one and that SSBs should not affect the operational aspect of IIFS.
3. **Minimalist approach**, where authorities play a partial role in regulating Islamic finance. This approach is generally followed by regulators in Gulf Cooperation Council (GCC) countries, with the exclusion of Saudi Arabia.⁹⁰⁸

⁹⁰⁷ Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK."

⁹⁰⁸ Hasan does include Oman in this category, as Islamic finance was not allowed when he wrote his article. However, in 2011, the Central Bank of Oman (CBO) authorised Islamic banking and licensed two local banks to offer Islamic finance products. The CBO opted for a decentralised approach with regard to Shari‘ah governance in IIFS, and AAOIFI’s guidelines will be used. See Oman, "Islamic

IIFS are expected to have an appropriate Shari‘ah governance arrangement in place without being required to have a specific structure. The national authority is likely to study the rulings of international standards-setting bodies such as the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), whose governance standard is favoured in Bahrain, Dubai, and Qatar.

4. **Proactive approach**, which is applied in Malaysia, Sudan, Pakistan, Indonesia,⁹⁰⁹ and Brunei.⁹¹⁰ Authorities play a very active role in regulating Shari‘ah governance. A CSSB at the central bank operates as the final authority in Shari‘ah matters. IIFS are required to follow detailed instruction issued by the CSSB and also to appoint Shari‘ah supervisors at the institutional level. Supporters of this model strongly believe that this “regulatory-based approach” is the best way to regulate, design, and ensure Shari‘ah compliance.⁹¹¹

6.2.1. Justifications for CSSBs

Two main concerns have been raised about the need for CSSBs: establishing a CSSB can add another layer of cost, and a CSSB might slow the business activities of IIFS with bureaucratic procedures. Both of these concerns arise because such a national body is likely to study the ruling of international standards-setting bodies

Banking Regulatory Framework " The Central Bank of Oman (CBO),, <http://www.cbo-oman.org/news/IBRF.pdf>. accessed 20 May 2013; Bernardo Vizcaino, "Oman plans Islamic finance rules before year-end," Reuters, <http://in.reuters.com/article/2012/06/27/islamic-finance-regulation-idINL6E8EU1VI20120627>. accessed 10 March 2013

⁹⁰⁹ Humayon Dar, "Implementing Shari‘ah Governance -Awaiting Challenges" (paper presented at the Managing Shariah Risk through Shariah Governance, London, 10/8/2009).

⁹¹⁰ Hasan places Pakistan under a separate category titled “Interventionist Approach” due to the power of the Shari‘ah Federal Court over matters involving Islamic finance. However, because a central Shari‘ah board does exist at the State Bank of Pakistan, I opted to include it under the proactive approach.

⁹¹¹ Hasan, "Shari‘ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p114. It is worth noting that in Iran there are no SSBs at the institution level, because the whole banking system is assumed to be interest-free. The sole authority on Shari‘ah matters seems to be the Council of Guardians, which is a separate entity from the Central Bank of Iran.

such as the AAOIFI, the International Fiqh Academies, the International Shari'ah Research Academy for Islamic Finance (ISRA), and the Islamic Financial Services Board (IFSB) prior to issuing its binding opinion.⁹¹² This process could seriously affect product innovations and competition in the financial market. Nevertheless, supporters of a CSSB argue that it is important to protect the interests of depositors, investors, and shareholders who can be affected by the decisions of SSBs.⁹¹³ A CSSB with a strong mandate would add another layer of protection to stakeholders by overseeing the work of SSBs at IIFS. It would define a framework with clear duties and responsibilities for SSB members and IIFS management. It would also have the power to hold SSB members accountable for their wrongdoing, which would make take extra care with their deliberations, decision-making, and auditing tasks.

Moreover, a CSSB would help to maintain stability and confidence in the financial system by counteracting inconsistency in SSB decisions, which can shake the credibility of the Islamic finance industry by leaving stakeholders confused about which products are Shari'ah compliant and which are not, and about what Shari'ah compliance means. Chapter four of this thesis suggested that standardising the practise of Islamic finance by means of a defined authority can resolve this issue.⁹¹⁴ A CSSB is the most appropriate body to conduct this task, as is the case in Malaysia and Sudan.

In addition, establishing a CSSB would boost good governance practises on individual SSBs. Hasan⁹¹⁵ studied SSB governance practises in Malaysia, GCC, and

⁹¹² Opalesque, "Discussion Board: Country versus Bank Shariah Boards," Opalesque, http://www.opalesque.com/OIFI112/Discussion_Board_Country_versus_Boards579.html. accessed 10 December 2012

⁹¹³ Aldohni, "Islamic Banking Challenges Modern Corporate Governance: The Dilemma of The Shari'a Supervisory Board."

⁹¹⁴ See 4.5: Remedies for Inconsistency, p123

⁹¹⁵ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p310.

the UK and categorised their practises into five levels: underdeveloped practise, emerging practise, improved practise, good practise, and best practise. Hasan concludes that the average score of IIFS Shari‘ah governance in Malaysia falls into the “good practise” category, while the average scores of IIFS in GCC countries and the UK fall into the “emerging practise” and “improved practise” categories, respectively. Hasan attributes the good governance practises in Malaysia to its strong Shari‘ah governance framework and to the regulatory authority’s proactive approach. He suggests that less interference from regulators leads to weaker governance cultures. He further argues that simply establishing a Shari‘ah governance framework would not be sufficient to improve the governance practises in the market; rather, “supervision and enforcement are essential to ensure compliance with the existing rules”.⁹¹⁶ IIFS cannot be expected to “develop and portray strong Shari‘ah governance practises voluntarily and without proper supervision”, given the immaturity of the Islamic finance industry and the lack of motivation to implement these practises.

Finally, Shari‘ah is one of the main sources of the law in most Islamic countries. In some countries such as Saudi, any rules that contradict Shari‘ah are deemed unconstitutional.⁹¹⁷ Al-Ba‘ī⁹¹⁸ argues that this situation provides a strong justification for establishing a CSSB to oversee IIFS transactions and ensure a general compliance with Islamic law.

⁹¹⁶ Ibid., p312.

⁹¹⁷ Saudi Arabia, "The Basic Law of Governance," <http://www.mofa.gov.sa/sites/mofaen/aboutKingDom/SaudiGovernment/Pages/BasicSystemOfGovernance35297.aspx>. accessed 11 May 2013 Article 7

⁹¹⁸ ‘Abd āl-Ḥamid al-Ba‘ī, "Tanẓīm al-‘alāqah ban al-Maṣārif al-Islāmiyyah Wa al-Bunūk al-Markaziyyah Wa al-Bunūk al-Taqlīdiyyah al-Ukhrah" (paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005), p437.

6.3. Tasks of CSSBs

CSSBs have no standard set of tasks; their role can vary from one country to another.⁹¹⁹ Supporters of establishing a CSSB disagree on the tasks which should be assigned to it. On the one hand, it could be limited to overseeing the process of appointing SSB members and the procedure of approving new products. On the other hand, its mandate could be widened to include holding SSB members accountable, setting compulsory standards, and approving products. A survey of the literature suggests the following duties for central Shari‘ah supervisory boards⁹²⁰.

1. Setting Shari‘ah standards and rules for financial transactions. SSBs at the institution level can make *ijtihad* on the condition that it does not conflict with these standards.
2. Setting the framework which regulates the governance of SSBs, including the mechanisms of appointing their members and determining their remuneration as well as reviewing cases of conflict of interest.
3. Setting the standard and the process of internal Shari‘ah review within Islamic financial institutions (IFIs).
4. Overseeing the processes of converting conventional financial institutions into fully flagged IFIs.
5. Issuing Shari‘ah rulings on financial issues referred to it from different bodies including the central bank, SSBs, and arbitrators.
6. Promoting coordination, collaboration, integration, and the exchange of Shari‘ah opinions among SSBs.

⁹¹⁹ Opalesque, "Discussion Board: Country versus Bank Shariah Boards".

⁹²⁰ See for example: Fidād, "al-Raqābah al-Shar‘iyyah Wa Dawruhā Fī Dabṭ A‘māl al-Maṣārif al-Islāmiyyah," p19. Yūsuf ‘AbdAllāh al-Shabīlī, "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif: Dawābiṭhā Wa Aḥkāmhā Wa Dawrhā fī Dabṭ ‘Amal al-Maṣārif" (ibid.), p27-28; al-Muzaynī, "Tarshīd al-‘Amal Fī al-Ha‘āt al-Shar‘iyyah Lil-mu‘assasāti al-Māliyyah al-Islāmiyyah," p23; Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services"; Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions."

7. Approving widely used contracts and new financial products which can be deemed shifts in the industry.
8. Issuing a report certifying each SSB's procedure of issuing *fatwas*.
9. Acting as a mediator to resolve disputes between an SSB and the IIFS management or board of directors.⁹²¹

In addition, a CSSB can function as a unit within the state central bank, as is the case in Malaysia, Sudan, and Pakistan, or under the supervision of a different entity, as is the case in Kuwait and UAE.⁹²² The former boards tend to be more active in practice than the latter. For example, in Kuwait and the UAE, the final authority in Islamic financial matters is a committee at the Ministry of Awqaf and Islamic Affairs.⁹²³ However, as Mashal notes,⁹²⁴ its supervision in Kuwait is limited because it only applies if there is a disagreement between the SSB members within one IIFS. In this situation, the management of the IIFS can refer the matter to the Fatwa Committee at the Ministry of Awqaf and Islamic Affairs. The CSSB in UAE, in theory, has a stronger mandate than the one in Kuwait. For example, it is tasked with conducting *ex post* Shari'ah audits⁹²⁵ on IIFS and approving the appointment of SSB

⁹²¹ Opalesque, "Discussion Board: Country versus Bank Shariah Boards".

⁹²² Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p391.

⁹²³ See: Kuwait, "Central Bank of Kuwait Law No. 30/2003 " CBK,, http://www.cbk.gov.kw/www/law_iii.html#ch3_10. accessed 8 September 2011, article 93 United Arab Emirates, "Federal Law No-(6) of 1985 concerning Islamic Banks and Financial Institutions and Investment Companies," Central Bank of United Arab Emirates,, <http://www.centralbank.ae/pdf/LawNo6-1985-IslaminBanks.pdf>. accessed 10 November 2011, Article 5.

⁹²⁴ Abdulbari Mashal, "khuṣūsiyyah wa Mutatalabāt al-Raqābah al-Shar'iyyah lil-Maṣarif al-Markazī 'alā al-Mu'asasāt al-Māliyyah al-Islāmiyyah" (paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, Bahrain, 27 - 28/5/2008), p15.

⁹²⁵ This thesis uses "Shari'ah review" and "Shari'ah audit" interchangeably. However, in some parts of the research, "Shari'ah review" has been used to refer to the Shari'ah assessment conducted by SSBs of IIFS, while "Shari'ah audit" has been used to refer to external Shari'ah assessment conducted by the general auditing committee in the IIFS or by an external party.

members as well as issuing a binding *fatwa* on certain cases. However, Mashal suggests that this central Shari‘ah committee is not active in practise.⁹²⁶

The description of central Shari‘ah boards in Sudan and Malaysia in the following sections offers a better understanding about the nature of CSSB work.

6.4. The Central Shari‘ah Board in Sudan

The case of the CSSB in Sudan tends to be overlooked in contemporary Islamic finance literature when discussing the role of regulators. The example of Malaysia is often pointed out, although Sudan has a very strong CSSB that predates the Malaysian one. This might be because Malaysia has more financial resources to showcase its experience. Moreover, the literature may focus on the Malaysian approach because unlike Sudan, which Islamised its whole financial system in 1991,⁹²⁷ Malaysia regulates Islamic finance alongside conventional finance in a dual financial system.⁹²⁸ A key reason to shed the light on the CSSB in Sudan is its explicit charge to prevent creative Shari‘ah compliance,⁹²⁹ which makes it highly relevant to the discussion in this thesis.

The Higher Sharia Supervisory Board for Banks & Financial Institutions (HSSB)⁹³⁰ was the first CSSB worldwide. The experience of the CSSBs in Malaysia, Pakistan, and Bahrain was highly influenced by the experience of the Sudanese HSSB.⁹³¹ In fact, Bank Negara Malaysia (BNM) appointed the Secretary General of

⁹²⁶ Mashal, "khuṣūṣiyyah wa Mutatalabāt al-Raqābah al-Shar‘iyyah lil-Maṣarif al-Markazī ‘alā al-Mu’asasāt al-Māliyyah al-Islāmiyyah," p16.

⁹²⁷ Magda Ismail Abdel Mohsin, "The Practice of Islamic Banking System in Sudan," *Journal of Economic Cooperation* 26, no. 4 (2005): p30.

⁹²⁸ Obiyathulla I. Bacha, "Dual Banking Systems and Interest Rate Risk for Islamic Banks," *The Journal of Accounting, Commerce & Finance* 8, no. 1 (2004).

⁹²⁹ Sudan, "The Banking Business Organisation Act (2003)," CBOS,, <http://www.cbos.gov.sd/en/node/434>. accessed 27 May 2013 , Chapter 3.

⁹³⁰ This is the translation found at the central bank and on the HSSB website. However, the English version of The Banking Business (Organization) Act, 2003 translated it as the Higher Sharia Commission of Control on Banks and Financial Institutions.

⁹³¹ The Higher Sharia Supervisory Board for Banks & Financial institutions (HSSB), *Nash’at Wataṭawwur Wataqwīm Ha’āt al-Riqābah al-Shar‘iyyah fī al-Jihāz al-Maṣrifī al-Sūdānī* p75.

the Sudanese HSSB as a member of its Shari‘ah Advisory Council.⁹³² The HSSB was first established by the Sudanese finance minister’s decision in 1992. This decision was later incorporated into the Banking Business (Organisation) Act of 2003.⁹³³ This act states that the HSSB is an independent body whose members are appointed by a presidential decision in consultation with the finance minister.⁹³⁴ It is to consist of seven to 11 part-time employees who are experts in Shari‘ah, economics, banking, and law. The majority must be Shari‘ah scholars. The Banking Business (Organization) Act defines four objectives of the HSSB:

1. Issuing Shari‘ah *fatwas* and guidelines to unify the Shari‘ah bases of the banking and financial industries.
2. Auditing the policies and performance of the Central Bank, and the activities of banks and financial institutions, to insure they are in line with the law and the objectives of Shari‘ah, as well as with Islamic economic principles.
3. Refining the laws, regulations, and guidelines of the Central Bank, banks, and financial institutions to prevent any usurious transactions or hidden legal ruses, as well as anything that might result in consuming the people’s wealth counter to Shari‘ah law.
4. Working with the relevant authorities to develop and implement Islamic structures for transactions which are appropriate to all financing needs, as well as developing financial instruments suitable for the secondary market.

Moreover, the Banking Business (Organization) Act of 2003 assigns six functions to the HSSB⁹³⁵:

⁹³² Ibid.

⁹³³ Sudan, "The Banking Business Organisation Act (2003)". Chapter 3.

⁹³⁴ Ibid.

⁹³⁵ Ibid.

1. Forming and expressing an opinion on matters brought to its attention by the finance minister, the Central Bank governor, bank managers, or other stakeholders, and issuing related *fatwas*, recommendations, and advice.
2. Assisting IIFS and the auditing control unit at the Central Bank in performing their duties in accordance with the provisions of Shari‘ah.
3. Assisting the Central Bank and IIFS in developing and implementing training programs to teach the staff of these entities about banking and Islamic jurisprudence.
4. Assisting research departments in developing academic research and encouraging publication which serves its goals and duties.
5. Addressing any Shari‘ah disputes that arise between the parties subject to the articles of this Act and their clients, and issuing related *fatwas* and recommendations.
6. Performing any other functions that the HSSB deems necessary to achieve its objectives, subject to the approval of the finance minister.

A few additional privileges apply to the HSSB. The *fatwas* of the HSSB in banking-related matters are binding upon the Central Bank and IIFS unless challenged in court. However, the HSSB has no jurisdiction over any case submitted before the courts or in which a ruling has been issued by the relevant court.⁹³⁶ In addition, the HSSB can summon any employees or clients of an IIFS if it deems it necessary. It can also request documents and inspect the activities of IIFS either directly or via the central bank.⁹³⁷ One interesting example illustrating the authority of the HSSB is its 1995 decision to seize the non-Shari‘ah-compliant income of a Sudanese bank and

⁹³⁶ Ibid.

⁹³⁷ Ibid.

give the bank the right to appeal.⁹³⁸ This decision is understandable given the completely Shari‘ah-compliant financial system in Sudan, but it is highly difficult to apply it in other Islamic countries.

However, despite the act’s clear statement that the HSSB is independent, the HSSB budget, the terms of service of its Secretary General, and the remuneration of its members are determined by the finance minister in consultation with the Central Bank governor. This relationship could affect the independence of the HSSB, since it is tasked with auditing the Shari‘ah compliance of the Central Bank. Indeed, the relationship between the HSSB and the Central Bank is not entirely clear. Is the HSSB working as a subunit of the Central Bank and reporting to its governor? What is the status of its resolutions in practise if they conflict with the Central Bank governor’s view? In addition, despite the strong mandate of HSSB, this mandate notably does not specify its authority to license SSB members. A survey conducted by the HSSB⁹³⁹ shows that the appointment of 60% of SSB members in Sudan was not subject to the approval of the HSSB. Moreover, there seems to be ambiguity in practise regarding the relationship between the HSSB and individual SSBs. In the same survey mentioned earlier, 65% of SSBs in Sudanese banks deemed their relationship with the HSSB a coordinating one, while 25% of SSBs deemed it obligatory and 10% regarded it as advisory.⁹⁴⁰

6.5. The Central Shari‘ah Board in Malaysia

The centralised approach of Shari‘ah governance at Bank Negara Malaysia is of particular interest because Malaysia—unlike Sudan—has dual systems of conventional and Islamic finance. In addition, the Malaysian approach is relevant to

⁹³⁸ The Higher Sharia Supervisory Board for Banks & Financial institutions (HSSB), *Nash’at Wata’awwur Wataqwim Ha’at al-Riqābah al-Shar’iyyah fī al-Jihāz al-Maṣrifī al-Sūdānī* p86.

⁹³⁹ Ibid., p120.

⁹⁴⁰ Ibid., p119.

this thesis's focus on the UK because Malaysian law is generally based on the common law system,⁹⁴¹ and because Malaysia managed to integrate Islamic finance practises within a legal system that is not originally based on Shari'ah. The BNM has taken a gradual approach towards regulating Islamic finance since the Central Bank of Malaysia Act in 1958 up to the 2009 Central Bank of Malaysia Act.⁹⁴² Today, Malaysia has one of the most sophisticated Shari'ah governance systems in the world.⁹⁴³ There are two national Shari'ah boards in Malaysia: the Shari'ah Advisory Council of Bank Negara Malaysia (SAC of BNM) and the Shari'ah Advisory Council of the Securities Commission (SAC of the SC).⁹⁴⁴ The BNM established its SAC in 1997, and in 2009, based on section 51 of the Central Bank Act, it made the SAC the sole authority in determining Shari'ah matters for any financial activities regulated by the BNM, such as Islamic banking and *takaful*⁹⁴⁵ business.⁹⁴⁶ The SC established its SAC in 1996 in accordance with section 18 of the Securities Commission Act (1993)⁹⁴⁷ for the purpose of advising the SC and ensuring the Shari'ah compliance of the Islamic capital market.⁹⁴⁸ This means that neither the SAC of the SC nor any financial institutions regulated by it are obligated to follow the resolutions that the SAC of BNM issues. In theory, the existence of two national Shari'ah boards could

⁹⁴¹ See: Malaysia, "Civil Law Act 67 (1956),," The Commissioner of Law Revision, Malaysia, <http://www.agc.gov.my/Akta/Vol.%202/Act%2067.pdf>. accessed 10 May 2013 Section 3 & 5.

⁹⁴² Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p85.

⁹⁴³ See about the Shari'ah governance in Malaysia: Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK."

⁹⁴⁴ Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p85.

⁹⁴⁵ Takaful is defined as a "mutual guarantee provided by a group of people against a defined risk or catastrophe befalling one's life, property or any form of valuable things." Syarikat Takaful Malaysia Berhad, "Glossary of Takaful," <http://www.takaful-malaysia.com.my/corporate/takafuloverview/pages/glossarytakaful.aspx>. accessed 11 April 2014

⁹⁴⁶ Malaysia, "(ACT 701) Central Bank of Malaysia Act".

⁹⁴⁷ "Securities Commission Act 498 (1993)," Securities Commission <http://www.sc.com.my/eng/html/resources/guidelines/SCA2005.pdf>. accessed 10 May 2013

⁹⁴⁸ Hakimah Yaacob, "The New Central Bank Of Malaysia Act 2009 (Act 701): Enhancing The Integrity And Role of The Shariah Advisory Council (SAC) in Islamic Finance," *ISRA Research paper 6/2010*.(2010) <http://www.kantakji.com/fiqh/Files/Markets/B103.pdf> accessed 10 May 2013

lead to conflicting views. However, in practise, the juristic resolutions of the two boards show small differences in their Shari'ah view.⁹⁴⁹ This similarity is mainly attributed to the fact that the two SACs are chaired by the same person and consist generally of the same members.⁹⁵⁰ This significant overlap raises the question of whether it would be more efficient to update the law and have a single national Shari'ah advisory board.

The functions of the SAC of BNM and SAC of the SC are almost identical, with the latter specialising in issues related to the Islamic capital market. Section 52 of the Central Bank of Malaysia Act 2009 states the following main tasks of SAC of BNM:

1. To ascertain the Islamic law on any financial matter and issue a ruling upon reference made to it in accordance with the relevant part of the Act;
2. To advise the Bank on any Shari'ah issue relating to Islamic financial business, the activities or transactions of the Bank;
3. To provide advice to any Islamic financial institution or any other person as may be provided under any written law; and
4. Such other functions as may be determined by the Bank.⁹⁵¹

In addition, section 56(1) of Central Bank of Malaysia Act 2009 and Section 316F of the CMSA assign a new function to both SACs. If a Shari'ah question arises before a court or an arbitrator in a case related to Islamic finance, then the court or the arbitrator must consider any published ruling of the SACs or refer the question to the

⁹⁴⁹ Ibid., p11.

⁹⁵⁰ Ibid. Securities Commission, "Members Of The Sc's Shariah Advisory Council," SC., <http://www.sc.com.my/main.asp?pageid=251&menuid=277&newsid=&linkid=&type>. accessed 15 May 2013; Bank Negara Malaysia (BNM), "Profile of current SAC members (2010 - 2013)," BNM., <http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802>. accessed 16 May 2013

⁹⁵¹ Malaysia, "(ACT 701) Central Bank of Malaysia Act "; "Capital Markets and Services Act 2007 (CMSA)," Securities Commission., <http://www.sc.com.my/eng/html/cmsa/cmsa2007/cmsa2007.pdf>. accessed 29 May 2013 Section 316B

appropriate SAC for a binding ruling. However, Yaacob⁹⁵² questions whether a civil judge can be compelled to refer a question to an SAC or to comply with its decision. In other words, what would happen if the judge declined to adhere to the SAC ruling? Theoretically, there seem to be legal justifications for the court to do so. The judge, for example, might rely on section 5 of the Civil Law Act 1956, which makes the English law the applicable law to commercial matters in the absence of any other written law.⁹⁵³ In addition, according to the Federal Constitution of Malaysia, the court is the highest body which can determine right and the wrong in a particular case.⁹⁵⁴ The court is not constitutionally allowed to relinquish this right by yielding to the ruling of a lower body such as the SAC of BNM or the SAC of the SC.⁹⁵⁵

The issue of creative Shari'ah compliance at hand does not seem to be a main concern of the SAC of BNM, in contrast with the central Shari'ah board in Sudan. According to Yaacob,⁹⁵⁶ when a product is submitted before the SAC or an SSB at the IIFS level, Shari'ah scholars will base their decision on the theoretical description presented; they will not investigate how this product is likely to be implemented in practise. As mentioned in chapter five,⁹⁵⁷ one cause of creative Shari'ah compliance is that some IIFS deliberately present their product in a way which ensures the approval of Shari'ah scholars, though in practise the product is not Shari'ah compliant.⁹⁵⁸

But is it permissible from a Shari'ah point of view for SSB members to approve products based on IIFS presentations without taking into account how they will be

⁹⁵² Yaacob, "The New Central Bank Of Malaysia Act 2009 (Act 701): Enhancing The Integrity And Role of The Shariah Advisory Council (SAC) in Islamic Finance". p14.

⁹⁵³ Malaysia, "Civil Law Act 67 (1956)", . , section 5

⁹⁵⁴ *Shamil Bank Bahrain v. Beximo Pharmaceuticals Limited & Ors [2003] EWHC 2118*,,(2003).

⁹⁵⁵ Yaacob, "The New Central Bank Of Malaysia Act 2009 (Act 701): Enhancing The Integrity And Role of The Shariah Advisory Council (SAC) in Islamic Finance". p15.

⁹⁵⁶ Ibid., p18.

⁹⁵⁷ See: p191

⁹⁵⁸ Abd Jabbar, "The Governance of Shari'a Advisers of Islamic Financial Institutions: The Practice in Malaysia," p313; Zighībah "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Ḥulūl Muqtarahah " p24.

implemented in reality? A well-established principle in *fatwa* literature is that a *maftā* (the scholar who issues a *fatwa*) needs to take into account the consequences of the *fatwa* before issuing it.⁹⁵⁹ Put differently, a Shari‘ah scholar is required to consider what actions may be taken based on his *fatwa*. Approving a particular product which is Shari‘ah compliant on paper but not in practise does not comply with this principle, because people are going to buy this product based on this *fatwa* and, in doing so, unwittingly deal with a non-Shari‘ah-compliant product.

There is also a question about the lack of a clear mechanism to hold SAC members accountable.⁹⁶⁰ In other words, who is “guarding the guardians” to make sure they are not abusing their position? Section 87 of the Central Bank Act protects any employee of the bank or any person appointed under the Act, such as SAC members, from liability as long as their actions were made in a good faith.⁹⁶¹ It is not clear how “good faith” might be interpreted; what standard of care does a scholar need to meet to be deemed as acting in good faith? For example, can one fail to investigate how a product will be implemented in practise and still satisfy the standard of acting in good faith? Does this fulfil the duty of the SAC set forth in section 52, “to ascertain the Islamic law on any financial matter and issue a ruling”? Arguably, the current legal provisions in the Central Bank of Malaysia Act 2009 and the Capital Markets and Services Act 2007 do not provide a sufficient mandate to prevent the practise of creative Shari‘ah compliance.

6.5.1. BNM Shari‘ah Governance Framework for Islamic Financial Institutions

To fully understand the functions of the SAC of BNM, it is important to consider the Shari‘ah Governance Framework for Islamic Financial Institutions issued by the

⁹⁵⁹ See: Ibrāhīm Mūsā al-Shāṭibī, *al-Muwāfaqāt*, ed. Mashhūr Ḥasan Salmān, vol. 5 (Dār Ibn ‘Affān, 1997), 177.

⁹⁶⁰ Yaacob, "The New Central Bank Of Malaysia Act 2009 (Act 701): Enhancing The Integrity And Role of The Shariah Advisory Council (SAC) in Islamic Finance". p23-24.

⁹⁶¹ Malaysia, "(ACT 701) Central Bank of Malaysia Act".

BNM. To that end, this part of the chapter outlines this document, which provides the most comprehensive Shari‘ah governance framework in the world. It ensures that sound Shari‘ah governance is accomplished by establishing a central Shari‘ah board and an SSB at every Islamic financial institution.⁹⁶² The framework aims to spell out how the BNM expects IFIs to arrange Shari‘ah governance to ensure the Shari‘ah compliance of all their activities.⁹⁶³ It also aims to inform the different parties involved in Shari‘ah governance (i.e., the board of directors, IFI management, and SSB members) of how they can fulfil their responsibility in relation to Shari‘ah and delineate the tasks of different units that the framework requires.

The framework consists of six sections, dealing mostly with the governance issues raised in chapter five.⁹⁶⁴ Section one highlights the overall requirements of the Shari‘ah governance framework and its main structures. Section two deals with the accountability and the duties of the board of directors, IFI management, and Shari‘ah committees.⁹⁶⁵ Section three is intended to protect the independence of the Shari‘ah committee; it outlines the role of the board of directors in this regard. Section four deals with the competence issue.⁹⁶⁶ It outlines the required qualifications of persons involved in implementing the framework to ensure their capability of undertaking such task, and it asks IFIs to have an official procedure in place for evaluating Shari‘ah committee members individually. The assessment should cover the members’ knowledge, competence, input, and effectiveness. Section five tackles confidentiality and consistency issues. It establishes the minimum rules which protect

⁹⁶² Bank Negara Malaysia (BNM), "Shari‘ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p1.

⁹⁶³ Ibid., p2.

⁹⁶⁴ Ibid., p4.

⁹⁶⁵ Appendix 4 provides more details about the duties, responsibilities, and accountability of the Shari‘ah Committee. Ibid., p29.

⁹⁶⁶ Appendix 2 outlines in detail the "Fit and Proper" criteria of the Shari‘ah Committee and the process of disqualifying SSB members.

the confidentiality of the financial institutions and ensure a degree of regularity in Shari'ah committee rulings. Section six focuses on Shari'ah compliance and research tasks. It sets the duties of four units which IFIs are required to establish, namely, units for internal Shari'ah review, Shari'ah auditing, Shari'ah risk management, and Shari'ah research.

The internal Shari'ah review is a regular evaluation undertaken by Shari'ah officers to ensure that IFI activities are in line with Shari'ah. The task includes suggesting corrective actions to solve noncompliance and governance processes to prevent repetition of any problems.⁹⁶⁷ The Shari'ah audit is a periodic evaluation (at least once a year, depending on the risk profile of the IFI) that independently examines the compliance level in IFI business operations and the effectiveness of internal control mechanisms for Shari'ah compliance.⁹⁶⁸ The audit should pay special attention to IFI financial statements; review the organisation's structure, people, processes, and IT system for compliance with regulatory requirements; and assess whether the IFI's Shari'ah governance procedure is adequate.⁹⁶⁹ The BNM has the power to appoint, at the expense of an IFI, a third party to undertake a Shari'ah audit on IFI activities if the BNM deems this action to be in the IFI's interest.⁹⁷⁰

The Shari'ah risk management unit is tasked with detecting and controlling any potential Shari'ah non-compliance risks which need to be mitigated to prevent the IFI's exposure to intolerable risk.⁹⁷¹ This unit is integrated with the IFI risk management structure, but as Shari'ah risk is more complex than conventional risk, and as its management requires a different knowledge base than the one used in

⁹⁶⁷ Bank Negara Malaysia (BNM), "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p23.

⁹⁶⁸ Ibid.

⁹⁶⁹ Ibid., p24.

⁹⁷⁰ Ibid., p25.

⁹⁷¹ Ibid.

managing risk in conventional finance, the task is assigned to risk officers with appropriate qualification in Shari‘ah.⁹⁷² Lastly, the Shari‘ah research unit is tasked with undertaking research on Shari‘ah issues. The framework also calls for it to distribute Shari‘ah rulings to the internal and external stakeholders.

The responsibility for setting up a strong Shari‘ah governance structure is clearly placed upon the IFI, and in particular on its board of directors.⁹⁷³ While the Shari‘ah committee is held liable and “accountable for all its decisions, views and opinions related to Shari‘ah matters”,⁹⁷⁴ the board of directors is responsible and accountable for the general governance of the institution. The IFI management is also responsible for implementing SAC and Shari‘ah committee decisions. Moreover, it bears the responsibility for identifying and referring any Shari‘ah matter to the Shari‘ah committee for a decision, as well as for providing the Shari‘ah committee with accurate and full information which the committee needs to consider before issuing its *fatwa*.⁹⁷⁵ The management is expected to provide adequate resources and a workforce appropriate to the size of the institution to implement the Shari‘ah governance framework. The guidelines further assert the management’s duty to “develop and adopt a holistic culture of Shari‘ah compliance within the organisation”.⁹⁷⁶

One notable feature of the framework is that it clearly states the procedure which the management ought to follow if they learn of non-Shari‘ah-compliant activities within the IFI. First, they should immediately notify the board of directors, the Shari‘ah committee, and the BNM. Secondly, the IFI should immediately stop engaging in new operations linked to the non- Shari‘ah-compliant business activities. Thirdly, they must draw up a plan to remedy the issue within 30 days of learning of

⁹⁷² Ibid.

⁹⁷³ Ibid., p5.

⁹⁷⁴ Ibid., p11.

⁹⁷⁵ Ibid., p12.

⁹⁷⁶ Ibid.

the incident.⁹⁷⁷ The plan should be jointly approved by the IFI board and its Shari‘ah committee. As a stopgap measure, when the BNM reasonably suspects that an IFI is undertaking non-Shari‘ah-compliant business activities, it is authorised to directly instruct the IFI to take rectifying action.⁹⁷⁸ In a further step to ensure Shari‘ah compliance, Shari‘ah committee members will not be in breach of the confidentiality and secrecy code if they report serious non-Shari‘ah compliance to the BNM in good faith.⁹⁷⁹

To prevent conflicts in SSB rulings which might undermine Shari‘ah compliance, the framework states that the Shari‘ah committee needs to follow a well-structured and documented procedure of Shari‘ah decision-making. Moreover, it strongly warns Shari‘ah committee members not to undermine SAC decisions. However, the Shari‘ah committee is permitted to follow a more strict Shari‘ah view than the SAC.⁹⁸⁰

Finally, the framework allocates an appendix to emphasising an important Shari‘ah compliance issue which was obscurely treated in the Central Bank Act of the BNM. It stresses that compliance with Shari‘ah should be maintained during all the stages of the product development process. It acknowledges that Shari‘ah non-compliance can happen in pre-approval phases (e.g., incorrect structuring of products) or post-approval phases (e.g., misrepresenting products in marketing or after offering them to clients). It also stresses that ensuring Shari‘ah compliance is a continuous process. The Shari‘ah committee must certify any new products and support its decisions with pertinent juristic reasoning and literature. Legal agreements and product documents must be checked in detail. Moreover, the appendix details the process followed in the pre-product approval and post-product approval phases. The

⁹⁷⁷ BNM has the right to extend this duration. *Ibid.*, p14.

⁹⁷⁸ BNM has the right to extend this duration. *Ibid.*

⁹⁷⁹ *Ibid.*, p20.

⁹⁸⁰ *Ibid.*

latter includes auditing the implementation of products in the market and conducting the internal Shari'ah review and Shari'ah governance auditing mentioned earlier in the framework.

One missing feature of the system is that new products are not submitted to the SAC of BNM for final approval. This might be intended to provide flexibility and speed to encourage market innovation. Nevertheless, seeking the approval of the SAC as a final stage before offering the product on the market might help to avoid conflicts in *fatwas* and maintain a standard rather than waiting for conflicting products to be offered on the market and cause a problem. One might argue that this problem is avoided by asking the Shari'ah committee to observe SAC rulings and decisions before approving products. Still, not all newly structured products have been addressed in SAC rulings and decisions.

Overall, however, the BNM offers a very well-structured Shari'ah governance framework which largely was adopted in the Islamic Financial Services Board standards for best practises of Shari'ah governance.

6.6. UK Regulators' Approach towards Shari'ah Governance

As discussed above, a form of central Shari'ah supervisory board (CSSB) with strong legal power acting within a Shari'ah governance framework would be an ideal solution to strengthen Shari'ah compliance in the Islamic finance industry. However, this remedy might not be desirable in some countries for various reasons. Wilson⁹⁸¹ suggests that former Financial Services Authority (FSA) in the UK was hesitant to follow the Malaysian approach of a centralised Shari'ah board because of the sensitivity of giving less decision-making power to individual SSB members. Yahia⁹⁸²

⁹⁸¹ Wilson, "Regulatory Challenges Posed by Islamic Capital Market Products and Services."

⁹⁸² Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p79.

suggests another reason that central bankers should not regulate Shari‘ah governance: requiring an official board that is tasked with applying a particular religious law might result in religious discrimination lawsuits brought by consumers following other religions. Most importantly, UK regulators deem establishing a central Shari‘ah board a religious matter that is beyond the legal authority of a secular regulator.⁹⁸³

Many researchers summarise the attitude of the UK regulatory authority towards regulating Islamic finance by quoting Callum McCarthy, the chairman of the former Financial Services Authority: “No obstacles, no special favours”.⁹⁸⁴ However, a 2003 speech by Michael Foot, then the managing director of the FSA, stressed the importance of explaining the nature of the product to the consumer who is buying it, and emphasised that product providers must comply with basic EU Directive requirements for consumer protection. The FSA, Foot said, would ensure sufficient disclosure during transactions. He further stated that the FSA would

no doubt continue to play that role in respect of sharia’a compliant products too (and in some case our rules will leave us no choice). However, I think it is also true to say that we shall be looking for help from experts wherever we can find them. And I should also add – though it is probably unnecessary for me to say this – we shall have neither the ability nor the desire to monitor a bank’s actual sharia’a compliance. That has to be something for the sharia’a board and for the institution itself.⁹⁸⁵

This statement was made during the early days of implementing Islamic finance products in the UK. However, the position of the FSA did not change much with regard to Shari‘ah governance, as can be seen in its 2007 paper titled “Islamic Finance in the UK: Regulation and Challenges”. The FSA seemed to be keen on stressing its nature as a secular authority and leaving the responsibility for ensuring

⁹⁸³ H. M. Treasury, "The Development of Islamic Finance in the UK the Government's perspective" p19.

⁹⁸⁴ Callum McCarthy, "FSA encourages growth of Islamic finance in the UK," FSA, <http://www.fsa.gov.uk/library/communication/pr/2007/121.shtml>. accessed 10 May 2013

⁹⁸⁵ Michael Foot, "The Future of Islamic Banking in Europe," FSA, <http://www.fsa.gov.uk/library/communication/speeches/2003/sp150.shtml>. accessed 10 May 2013

Shari'ah compliance to the IIFS, and the Financial Conduct Authority (FCA) which replaced the FSA in 2013 has followed in its footsteps in this regard.⁹⁸⁶ The FSA seemed to be aware of some of the issues in the industry, such as the lack of standardisation and possibility of Shari'ah arbitrage, and to recognise that ensuring Shari'ah compliance is a continuing process. However, Zulkifli Hasan⁹⁸⁷ notes that the Shari'ah governance practises of several financial institutions in the UK show that IIFS are entirely free to arrange their Shari'ah governance without subjection to regulatory policies or guidelines.

Similarly, in 2008, HM Treasury published a document outlining the government's perspective on the development of Islamic finance in the UK.⁹⁸⁸ It stresses the treasury's aim to regulate Islamic finance to the same standard achieved in conventional finance and pledges that regulators will act to ensure that Islamic finance consumers enjoy the same level of advice and transparency available to conventional finance consumers.⁹⁸⁹ It also emphasises the importance of international standards and that these standards should be accessible to those who need it in IIFS. It states that the UK authorities have a good relationship with international Islamic standard-setting bodies and meet with them on equal terms, follow their recent developments, and attends their conferences.⁹⁹⁰ However, the responsibility for assuring consumers about the authenticity of Shari'ah-compliant products is placed on the Islamic finance sector. The document clearly shows that the government does not plan to follow a state-led approach taken by other countries such as Malaysia.⁹⁹¹ This is because the authorities in the UK regard themselves as secular bodies and think that

⁹⁸⁶ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*.

⁹⁸⁷ Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p104.

⁹⁸⁸ H. M. Treasury, "The Development of Islamic Finance in the UK the Government's perspective".

⁹⁸⁹ Ibid., p18.

⁹⁹⁰ Ibid., p21.

⁹⁹¹ Ibid., p19.

such a rigid approach could slow development in the industry and further fragment the market, especially for IIFS active in more than one jurisdiction.

Two main questions need to be addressed in this area. First, is the process of ensuring Shari‘ah compliance in fact a private religious matter beyond the power of a secular financial regulator? And how does requiring IIFS to establish a Shari‘ah auditing unit that checks for adherence to an international standard conflict with the secular nature of a regulator? Wilson⁹⁹² acknowledges that central banks and regulators are not able to bear the responsibility for Shari‘ah compliance. However, he believes that they are responsible for making sure that an adequate process for ensuring Shari‘ah compliance exists in financial institutions. In addition, these entities should familiarise themselves with the implications of Islamic finance and promote efforts towards following international Shari‘ah standards. Moreover, they should be concerned with corporate governance issues, which include examining the power of the SSB, and their duties towards consumers and IIFS management.

The second question in this area is whether regulators, by not regulating Shari‘ah governance (and not trying to prevent creative Shari‘ah compliance in IIFS), are fulfilling their obligation to protect consumers, one of the main objectives of any financial regulator.⁹⁹³ A study funded by the Dutch Central Bank suggests that Islamic financial consumers enjoy less protection than their counterparts in conventional finance.⁹⁹⁴ Consumer protection was one of the main regulatory objectives of the former Financial Services Authority, as is stated in the Financial Services and Markets Act 2000.⁹⁹⁵ The Financial Services Act 2012 shifted this duty to a newly established institution, the Financial Conduct Authority (FCA). Article 1B (3) of the

⁹⁹² Wilson, "Regulatory Challenges Posed by Islamic Capital Market Products and Services."

⁹⁹³ See: *ibid.*

⁹⁹⁴ Verhoef, Azahaf, and Werner, *Islamic Finance and Supervision: an Exploratory Analysis*, p32.

⁹⁹⁵ United Kingdom, "Financial Services and Markets Act 2000 : Chapter 8".

Act lists consumer protection as the first of the FCA's operational objectives,⁹⁹⁶ which is defined in section (1C) as "securing an appropriate degree of protection for consumers". To determine what is appropriate, the FCA must consider different factors such as the different degrees of risk associated with various types of products and transactions, the differing levels of experience and knowledge of consumers, the needs of consumers to access well-timed information that is fit for their purpose, and consumers' different expectations in regard to different types of investments or transactions. However, consumers, as a general principle, should be responsible for their decisions.

In line with the factors mentioned above, the question is to what extent the FCA has fulfilled its duty of consumer protection in the Islamic finance market. The explanatory notes of the 2012 Act suggest that the FCA can, for example, specify the way in which a service provider must disclose certain information to its consumers before entering into an agreement. It also can require certain elements which the provider advice should cover to ensure that it is not misleading. However, it is worth noting that these FCA objectives do not force a "statutory duty" upon the FCA to act to ensure an appropriate level of protection for all consumers. Rather, they give the FCA authority to act, for instance, to protect a single group of persons who can be included under the definition of "consumer".⁹⁹⁷

The FSA's 2012 annual report emphasised a new strategy for protecting consumers.⁹⁹⁸ The strategy was first devised in 2010, and the Business Plan of 2011/12 offered new details about how this strategy should be implemented. It

⁹⁹⁶"Financial Services Act 2012" p20.

⁹⁹⁷Parliament House of Lords, "Financial Services Bill : Explanatory Notes," TSO, <http://www.publications.parliament.uk/pa/bills/cbill/2010-2012/0278/en/2012278en.pdf>. accessed 25 May 2013 Note 85.

⁹⁹⁸Financial Services Authority, "Financial Services Authority Annual Report 2011/12," FSA,, <http://www.fsa.gov.uk/pubs/annual/ar11-12/ar11-12.pdf>. accessed 19 May 2013

acknowledged that the FSA needed to take a more proactive role to avert any problems for consumers. It pledged to focus on ensuring better access to information for consumers, as well as earlier, stronger regulatory intervention. The Business Plan suggested adopting a business model and strategy analysis to detect potential risks in firms' conduct which could be further examined via intensive supervision. Moreover, it continued, products would receive more attention, particularly in the design phase at firms, to ensure that they suited the needs of their targeted customers.⁹⁹⁹ This tactic aimed to avoid detriment to consumers at a very early time in the product's life cycle.¹⁰⁰⁰ The Business Plan also created a unit of Consumer Affairs to provide better engagement with consumers,¹⁰⁰¹ and it committed to taking tougher enforcement actions in cases of poor dealing with consumers and mis-selling.¹⁰⁰² The plan paid special attention to certain areas including structured products and mortgage advice, where most Islamic finance business is concentrated. As of 1 January 2013, the Retail Distribution Review (RDR) came into force, requiring firms to clearly explain their services and charges to consumers. The new rules also aim to improve the ethical code and the professional standards of investment advisers.¹⁰⁰³

However, Jonathan Ercanbrack¹⁰⁰⁴ points out some distinctive risks linked with Shari'ah-compliant products and criticises how financial regulators in the UK dealt with them. He argues that their reticence to regulate the religious aspect of these products and its equivalent regulatory treatment of the Islamic and conventional financial sectors inadequately mitigated the unique risk associated with Islamic finance, which occurs because the main motivation for Muslim consumers to buy

⁹⁹⁹ Ibid., p57.

¹⁰⁰⁰ Ibid., p53.

¹⁰⁰¹ Ibid.

¹⁰⁰² Ibid., p59.

¹⁰⁰³ Ibid., p48.

¹⁰⁰⁴ Ercanbrack, "The Regulation of Islamic Finance in the United Kingdom," p69-71.

these products is their Shari‘ah-compliant nature. The current regulatory approach of the FCA seems to ignore the reputational risks which can occur with these products.¹⁰⁰⁵

Similarly, Rider¹⁰⁰⁶ suggests that regulators in secular countries, such as the FCA in the UK and the Securities and Exchange Commission (SEC) in the US, are mainly concerned with the compliance of Islamic financial products with the standards for conventional products. The Islamic nature of the product is seen as an extra element. If an IIFS were offering as Shari‘ah-compliant a product that does not actually comply with Islamic law, it might be liable for breach of contract or misrepresentation. It could be also liable for mis-selling under various consumer protection laws and regulations. For example, the UK Consumer Protection from Unfair Trading Regulations 2008 prohibits “misleading actions” where wrong information is provided about the nature or the main features of a product which “causes or is likely to cause the average consumer to take a transactional decision he would not have taken otherwise”.¹⁰⁰⁷ Under this Act, the plaintiff needs to prove that the service provider has knowingly or carelessly undertaken the misleading action.¹⁰⁰⁸ Another relevant legislation in this regard is the Fraud Act 2006, which make it an offense for a person to gain or intend to gain money by deceitfully making a false representation. The representation, either expressed or implied, is deemed false “(a) if it is untrue or misleading, and (b) the person making it knows that it is, or might be,

¹⁰⁰⁵ The HM tax arrangement for Islamic financial products suggests that it is aware that the economic substance of these products does not differ from that of conventional ones. H. M. Treasury, "The Development of Islamic Finance in the UK the Government's perspective" p15.

¹⁰⁰⁶ Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," p136.

¹⁰⁰⁷ United Kingdom, "The Consumer Protection from Unfair Trading Regulations 2008," The National Archives, http://www.legislation.gov.uk/ukxi/2008/1277/pdfs/ukxi_20081277_en.pdf. accessed 16 May 2013

¹⁰⁰⁸ Ibid., p6.

untrue or misleading”.¹⁰⁰⁹ In addition, the act makes it an offense for a person to fail to disclose information that he is required by the law to disclose when he intends by doing so to make “a gain for himself or another, or to cause loss to another or to expose another to a risk of loss”.¹⁰¹⁰

Furthermore, according to the sixth principle of the FCA “Principles for Business”, firms are required to treat their clients fairly and pay attention to their interests.¹⁰¹¹ The FCA thus aims to ensure that consumers will receive “clear information, suitable advice and an acceptable level of service”.¹⁰¹² The FCA acknowledges that Shari‘ah-compliant products are sometimes based on complicated or uncommon structures, and therefore emphasises that IIFS should make sure their clients properly understand their products. This is particularly important at a time when many newly developed financial products are offered in the market.¹⁰¹³ Additionally, principle nine of the FCA “Principles for Business” states that “a firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment”.¹⁰¹⁴ Here, what matters is the suitability of the advice for the consumer, not the financial performance of the product. If the recommendation was suitable at the time of sale, and the risk involved was clearly explained to the consumer, negative return on the investment cannot by itself be a ground of claiming mis-selling.¹⁰¹⁵

¹⁰⁰⁹ "Fraud Act 2006 Chapter 35," The National Archives, http://www.legislation.gov.uk/ukpga/2006/35/pdfs/ukpga_20060035_en.pdf. accessed 10 May 2013, section 2.

¹⁰¹⁰ Ibid. section 3.

¹⁰¹¹ Financial Conduct Authority (FCA), "Principles for Businesses," FCA,, <http://media.fshandbook.info/content/full/PRIN/2/1.pdf>. accessed 10 May 2013

¹⁰¹² Ibid.

¹⁰¹³ Ainley et al., *Islamic Finance in The UK : Regulation and Challenges*, p22.

¹⁰¹⁴ Financial Conduct Authority (FCA), "Principles for Businesses".

¹⁰¹⁵ Financial Services Authority, "FSA advises industry on definition of "mis-selling"," FSA,, <http://www.fsa.gov.uk/library/communication/pr/2003/052.shtml>. accessed 9 May 2013

To what extent do providers of Islamic financial products comply with these requirements? Hainsworth¹⁰¹⁶ suggests that because of the different interpretations of Shari‘ah, it is unlikely that an IIFS would itself make a representation or provide advice with regard to the Shari‘ah compliance of particular products. Rather, international practise tends to reveal the names of SSB members who approved the products, as well as publishing their *fatwas*. For the same reason, Hainsworth also highly doubts that the relevant authority (now the FCA in the UK) would examine IIFS compliance with Shari‘ah.¹⁰¹⁷ He suggests that its focus would be directed towards the compliance of IIFS with governance standards published by the IFSB and AAOIFI. Although they are not legally binding, these standards may become relevant in assessing the compliance of an IIFS with this principle or other principles.¹⁰¹⁸

Nonetheless, with no adopted Shari‘ah standard, it would difficult to prove an offense under the various laws mentioned above. To overcome this problem, the Muslim Council of Britain (MCB), the Islamic Finance Council, and the Utrujj Foundation have published a draft of an Islamic Finance Transparency Standard.¹⁰¹⁹ The aim of this standard is not to standardise Shari‘ah per se, but rather to standardise the procedure for ensuring Shari‘ah compliance in a way that protects consumers.¹⁰²⁰ Due to the absence of Shari‘ah governance standards in the UK, the MCB and its partners raised concerns over the practise of some IIFS who are profiting from selling Shari‘ah -compliant products to the Muslim community without putting in place an

¹⁰¹⁶ Antony Hainsworth, *Islamic financial institutions and islamic finance* (London: LexisNexis, 2009), p85.

¹⁰¹⁷ *Ibid.*, p119.

¹⁰¹⁸ *Ibid.*

¹⁰¹⁹ The Muslim Council of Britain, "Islamic Finance Transparency Standard : a Consultation," MCB,, <http://www.mcb.org.uk/uploads/MCBIslamicFinanceTransparencyStandard.pdf>. accessed 9 May 2013

¹⁰²⁰ *Ibid.*, p13.

adequate process to ensure that these products and services do actually comply with Shari‘ah.¹⁰²¹

The Islamic Finance Transparency Standard also notes that existing international standards such as those of AAOIFI and IFSB are primarily known to practitioners.¹⁰²² When ordinary consumers buy Shari‘ah-compliant products, they cannot independently ensure that what is presented to them is actually Shari‘ah-compliant. It is improbable to assume that general consumers with no personal research would know which product best serves their interests. Given that the market is relatively new and lacks a published standard, ordinary consumers are vulnerable to abuse by dishonest service providers. Publishing and adopting a user-friendly standard would raise the awareness of consumers as well as removing suspicions of part of the Muslim community about the Shari‘ah authenticity of these products.¹⁰²³

As mentioned earlier, the FSA wanted consumers to be informed about the basis on which an IIFS presents itself as conducting Shari‘ah-compliant business. However, the research conducted by the MCB suggests that many IIFS have not communicated these grounds to their consumers.¹⁰²⁴ It further notes that the FSA did not taken any action in regard to this matter while it existed, notwithstanding that all financial institutions are required by law to advertise in “fair, clear and not misleading” ways.¹⁰²⁵ The MCB hopes that extensive compliance with the proposed standard in the market will help to reveal those IIFS that do not comply with this rule¹⁰²⁶

¹⁰²¹ Ibid., p6.

¹⁰²² Ibid.

¹⁰²³ Ibid., p7.

¹⁰²⁴ Ibid., p13.

¹⁰²⁵ Financial Services Authority, "Conduct of Business Sourcebook (COBS)," FSA,, <http://fshandbook.info/FS/html/handbook/COBS/4/2>. accessed 10 May 2013, Section 4.2: Fair, Clear and Not Misleading Communications.

¹⁰²⁶ The Muslim Council of Britain, "Islamic Finance Transparency Standard : a Consultation" p7.

The Islamic Finance Transparency Standard has been drafted so that it should not pose a challenging burden to market players or be seen by prospective service providers as a barrier to entry.¹⁰²⁷ After receiving feedback on the standard, the MCB aims to promote the standard's adoption by creating informal associations with community organisations and other relevant institutions. It also plans to design a stamp which IIFS can use to certify that they comply with the Islamic Finance Transparency Standard. The standard will be revised every two years to ensure that it accommodates the latest developments and practises in the market.¹⁰²⁸ The standard can be used by any financial institution offering Shari'ah-compliant products in the UK, provided that its products, documentation, and process have been verified by an independent competent Shari'ah expert. The name of that expert should be stated in all marketing material, and the expert's qualifications and the relevant *fatwas* should also be accessible on the IIFS website. Finally, a regular Shari'ah audit needs to be undertaken by a "Shari'ah expert(s) or other suitably qualified person" to ensure that implementation of the products is in line with Islamic law.¹⁰²⁹

However, it is not clear how the MCB will ensure that IIFS continually comply with the standard. How will it check whether a regular Shari'ah audit has been conducted? The language of the draft suggests that the financial institution will be responsible for complying with the standard without supervision by the MCB. Without establishment of a self-regulatory body, this standard may be abused by service providers and further harm the confidence of consumers in the market. This might be the case, taking into account that such a standard will be funded by the very institutions that use it. Moreover, since the draft of the standard was published on 6 October 2008, there have not been any publications in response to the consultation or any update.

¹⁰²⁷ Ibid., p8.

¹⁰²⁸ Ibid.

¹⁰²⁹ Ibid., p16.

In summary, the FCA's current approach with regards to Shari'ah governance is not adequate to protect consumers from creative Shari'ah compliance. The secular setting of the regulatory authorities in the UK should not hinder the FCA from ensuring that proper governance culture is adopted within SSBs. The FCA ought to strongly encourage IIFS and other relevant organisations in the UK to form a self-regulatory body for Islamic finance.¹⁰³⁰ In addition, other regulatory mechanisms discussed in chapter seven can be employed to protect vulnerable consumers from abuse by dishonest service providers.

6.7. Saudi Regulators' Approach towards Shari'ah Governance

The choice of the Kingdom of Saudi Arabia (KSA) as a reference is motivated by the fact that despite the huge and growing market for Islamic finance, which by the end of 2007 controlled over 75% of the finance market in Saudi Arabia,¹⁰³¹ specific regulation of the industry is non-existent, as neither the legal instruments nor the appropriate body exist to oversee the industry. Rodney Wilson¹⁰³² has observed that "the sensitive issue of Shari'ah compliance was not really addressed by SAMA [Saudi Arabian Monetary Agency]",¹⁰³³ nor was it tackled by the Capital Markets Law of 2003.¹⁰³⁴ These omissions are particularly ironic given the number of *sukūk* issuances

¹⁰³⁰ On 30 October 2013, Reuters reported the establishment of The Association of Sharia Scholars in Islamic Finance (ASSIF), a British-registered charity aiming to issue a professional code and Shari'ah guidelines. The researcher was not able to find a website for the ASSIF or any new information. See: Bernardo Vizcaino, "Islamic Scholars Launch Global Professional Association," Reuters <http://www.reuters.com/article/2013/10/30/islamic-finance-idUSL5N0IK3GG20131030>. accessed 2 March 2014

¹⁰³¹ al-Saud, "Siyāsah al-Jawdah al-Shar'īyyah fī al-Maṣrifīyah al-Islāmiyyah". p10.

¹⁰³² Rodney Wilson, "The Development of Islamic Finance in the GCC," (London: LSE Centre for the Study of Global Governance, 2009), p5-7.

¹⁰³³ Ibid., P5,7.

¹⁰³⁴ "Capital Market Law," Royal Decree No. (M/30), <http://www.cma.org.sa/En/AboutCMA/CMALaw/Documents/CAPITAL%20MARKET%20LAW-26-8-009.pdf>. accessed 25/09/2011

and hedge funds as well as large Shari‘ah-compliant mutual funds businesses in Saudi Arabia.¹⁰³⁵

Unlike in the UK, the regulation of Shari‘ah governance in Saudi is not hindered by the secular setting of the regulatory authorities. In fact, article one of the Basic Law of Saudi Arabia, which establishes the kingdom’s governing principles, states that Islam is the official religion and that the Quran and the *sunnah*, the two primary sources of Shari‘ah, are the constitution of Saudi.¹⁰³⁶ Article seven of the Basic Law states that the government derives its power from these two holy sources and that they are “rule over any State Laws”.¹⁰³⁷

Article two of the law of the Saudi Arabian Monetary Agency, which acts as the central bank of Saudi Arabia, further affirms the supremacy of Shari‘ah in Saudi law. It states that SAMA “shall not pay nor receive interest, but it shall only charge certain fees on services rendered to the public and to the Government, in order to cover the Agency's expenditures. Such fees shall be charged in accordance with a regulation passed by the Board of Directors and approved by the Minister of Finance”.¹⁰³⁸ Moreover, the law makes it clear that SAMA cannot act “in any manner which conflicts with the teachings of the Islamic Law. The Agency shall not charge any interest on its receipts and payments”.¹⁰³⁹ In reality, however, conventional finance is practised,¹⁰⁴⁰ and interest is legally enforced by the Banking Disputes Settlement Committee of SAMA, which has jurisdiction over any banking dispute in the KSA.

¹⁰³⁵ Wilson, "The Development of Islamic Finance in the GCC."; Hasan, "Regulatory Framework of Shari‘ah Governance System in Malaysia, GCC Countries and the UK."

¹⁰³⁶ Saudi Arabia, "The Basic Law of Governance".

¹⁰³⁷ Ibid.

¹⁰³⁸ Saudi Arabia, "Charter of the Saudi Arabian Monetary Agency," SAMA,, <http://www.sama.gov.sa/sites/samaen/RulesRegulation/BankingSystem/Pages/BankingSystemFD01.aspx>. accessed 12 May 2013

¹⁰³⁹ Ibid.

¹⁰⁴⁰ Hamad Al-Sayari, "Saudi Arabian Banking System & Capital Markets," SAMA, <http://www.sama.gov.sa/sites/samaen/News/Pages/News14230708.aspx>. accessed 10 May 2013

It is not clear why the Saudi regulator has so far been reluctant to introduce a framework for Shari‘ah governance and Islamic finance in general. Is it because they are not sufficiently convinced by the model of Islamic finance?¹⁰⁴¹ Is it because issuing a framework for Islamic finance officially acknowledges the existence of non-Shari‘ah-compliant practises? Or is it because SAMA does not see a need to regulate Islamic finance, since it is market driven? There is no official explanation or academic studies that clearly discuss this issue. Nevertheless, it seems that the authorities are hesitant to regulate Islamic finance due to the political sensitivity of such action or disclosure. The absolute monarchy system in Saudi Arabia seems to base its political legitimacy on enforcing Shari‘ah as a governing law.¹⁰⁴² Therefore, one might argue that the regime is keen to avoid any public action that might question its legitimacy. In fact, practicing usury is one of the justifications used by al-Qaeda and other radical groups to declare the Saudi state as non-Islamic or apostate and to justify its attacks.¹⁰⁴³

Ahmed Al-Saleh,¹⁰⁴⁴ the head of the legal department at SAMA, addresses this question by arguing that Islamic finance regulations have been introduced in other countries to resolve the obstacle of taxes which disadvantage Shari‘ah-compliant products on the market. In Saudi, Islamic finance products do not face any taxation issues; therefore, there is no need to introduce a specific Islamic finance framework.

¹⁰⁴¹ al-Nasser, "Wad' al-Maṣrifīyah al-Islāmiyyah Murbik Wa Naḥn Biḥajah ilā Wilādah Jadīdah".

¹⁰⁴² See article one from Saudi Arabia, "The Basic Law of Governance". Muḥammad al-Sa'īdī, "Qirā'ah Shar'īyyih fī al-Nizām al-Asāsī Lil-ḥukum," Lojainiat, <http://lojainiat.com/main/Content/%D9%82%D8%B1%D8%A7%D8%A1%D8%A9-%D8%B4%D8%B1%D8%B9%D9%8A%D8%A9-%D9%81%D9%8A-%D8%A7%D9%84%D9%86%D8%B8%D8%A7%D9%85-%D8%A7%D9%84%D8%A3%D8%B3%D8%A7%D8%B3%D9%8A-%D9%84%D8%AD%D9%83%D9%85-%D9%81%D9%8A-%D8%A7%D9%84%D9%85%D9%85%D9%84%D9%83%D8%A9-%D8%A7%D9%84%D8%B9%D8%B1%D8%A8%D9%8A%D8%A9-%D8%A7%D9%84%D8%B3%D8%B9%D9%88%D8%AF%D9%8A>. accessed 10 May 2013

¹⁰⁴³ See for example Abū Muḥammad 'Āṣim al-Maqdisī, *al-Kawāshif al-Jaliyyah fī Kufr al-Dawlah al-Su'ūdiyyah* vol. 2013 (al-Tawḥīd wa al-Jihād 2000), p26.

¹⁰⁴⁴ A personal interview with Dr Ahmed Al-Saleh on 9 April 2013. SAMA Headquarters, Riyadh Saudi Arabia.

In addition, Al-Saleh argues that Saudi is in essence an Islamic country with a free market, and the Islamic finance industry has been flourishing there over the last 25 years without the need to introduce special regulations for Islamic finance. When Al-Saleh was asked whether SAMA has a duty to protect consumers from being sold Shari'ah-compliant products which in reality do not comply with Shari'ah, he answered that SAMA's main concern is protecting depositors and ensuring that banks comply with the capital adequacy requirements. How banks repackage products for their customers is beyond the mandate of SAMA. If a client believes that he has been mis-sold a Shari'ah-compliant product, then he should submit his claim before the relevant court, which will examine the product based on the approval decision of the Shari'ah supervisory board of the bank in question. Answering a question about the role of SAMA in raising consumer awareness about the Shari'ah compliance of financial products, Al-Saleh said he believes that this function is also outside the scope of SAMA, as stated in its law. This task should be carried out by civil society organisations, not by SAMA.¹⁰⁴⁵

Al-Saleh's argument that Islamic finance regulations are only needed when there are tax issues for Shari'ah compliant products is not convincing. While this might be the case for some non-Islamic countries such as the UK, many Islamic countries such as Malaysia and Sudan have introduced Islamic finance regulations and Shari'ah governance frameworks, though they do not have any taxation obstacles to Islamic finance products. Shari'ah governance guidelines have been introduced in many countries with the aim of enhancing corporate governance values such as accountability and transparency across the Islamic finance industry and particularly on Shari'ah supervisory boards.

¹⁰⁴⁵ Ibid.

Many Islamic finance professionals in KSA also disagree with the view of Al-Saleh. Majed Alrasheed,¹⁰⁴⁶ head of the Shari‘ah unit at Bank Albilad, and Yaser Al-Marshdiy,¹⁰⁴⁷ head of the Shari‘ah Group of Alinma Bank (these institutions are two of the main fully-flagged Islamic banks in KSA), believe that the Islamic finance industry in Saudi is in need of a Shari‘ah governance framework. Sheikh Abdullah Bin Sulaiman Al Manea, one of the top Shari‘ah scholars within the Islamic industry and the chair of most SSBs in Saudi, even publicly criticised SAMA for being “one of the main obstacles preventing the Kingdom from being the centre of Islamic banking around the world”.¹⁰⁴⁸ He demanded that SAMA issue a specified framework for Islamic banking as is the case in conventional banking.

Given that current SAMA rules and regulations do not contain any specific provisions for Islamic finance or Shari‘ah governance, to what extent do they protect Saudi consumers from creative Shari‘ah compliance? Certain provisions within these regulations address consumer protection, corporate governance, conflicts of interest, and transparency.¹⁰⁴⁹ For example, the Implementing Regulations of the Law on Supervision of Finance Companies states that some provisions obligate finance companies to clearly describe the terms and type of a financing contract. It prohibits finance companies from issuing statements or presenting products in a way that can directly or indirectly misinform or deceive consumers.¹⁰⁵⁰ In addition, SAMA

¹⁰⁴⁶ A personal interview with Majed Alrasheed on 12 April 2013., Riyadh Saudi Arabia

¹⁰⁴⁷ A personal interview with Yaser Al-Marshdiy on 8 April 2013. Alinma Bank Headquarters, Riyadh Saudi Arabia

¹⁰⁴⁸ Husayn al-Wad‘ānī, "al-Manī‘ antaqīd "sāmā" wa uṭālibuhā bi" Maṣrifīyyih Islāmiyyih " Alwatan Online http://www.alwatan.com.sa/Economy/News_Detail.aspx?ArticleID=30871&CategoryID=2. accessed 10 May 2013

¹⁰⁴⁹SAMA, "Laws and Regulations," SAMA, <http://www.sama.gov.sa/sites/samaen/RulesRegulation/Pages/Home.aspx>. accessed 13 May 2013

¹⁰⁵⁰ See article 78 & 86 "Implementing Regulations of The Law on Supervision of Finance Companies (Arabic)" SAMA, [http://www.sama.gov.sa/sites/samaen/Finance/FinanceLib/L_EN_ImplementingRegulationsOfTheLawOnSupervisionOfFinanceCompanies\(Arabic\).pdf](http://www.sama.gov.sa/sites/samaen/Finance/FinanceLib/L_EN_ImplementingRegulationsOfTheLawOnSupervisionOfFinanceCompanies(Arabic).pdf). accessed 10 May 2013

published a draft of the principles for protecting bank clients, including general principles regarding fair trading, disclosure and transparency, financial education and awareness, and protection of the financial interests of clients. However, these general provisions do not adequately protect consumers who choose to buy Shari‘ah-compliant products on religious grounds. SAMA’s main concern, as Al-Saleh confirmed, seems to be financially protecting depositors rather than overseeing the Shari‘ah-compliant element of IIFS products. Although these provisions can be used by consumers to sue banks for mis-selling, SAMA ought to play a role in holding banks accountable for breaching consumer protection regulations, rather than relying on consumers to take legal action.

What is the best way to regulate Shari‘ah governance to strengthen Shari‘ah compliance in Saudi Arabia? As mentioned earlier, despite the growing business of Islamic finance in the Kingdom of Saudi Arabia, no legal framework surrounds the work of more than 50 SSBs in the KSA.¹⁰⁵¹ An IIFS voluntarily and unilaterally appoints a Shari‘ah supervisory board to review its products, and it and commits to implement *fatwas* and decisions issued by the SSB. The private sector has yet to form a strong self-regulatory body that compensates for SAMA’s lack of regulatory action. According to Majed Alrasheed,¹⁰⁵² a committee for Islamic finance has been established by banks offering Shari‘ah-compliant products in the kingdom. It holds four meetings per year which are attended by a representative from SAMA. The committee has not yet issued any guidelines or played an active role in terms of Shari‘ah governance. It has been trying to introduce an ethical guideline on the process of approving Shari‘ah-compliant products, and it also sometimes tries to

¹⁰⁵¹ ‘adlī Ḥamād, "Da‘wah Lījād Marji‘iyyah Shar‘iyyah Rasmiyaah Lisūq al-Māl Wālmaṣārif", *Okaz*, 19/8/2010 <http://www.okaz.com.sa/new/Issues/20100819/Con20100819368179.htm>. accessed 10 May 2013; al-Saud, "Siyāsah al-Jawdah al-Shar‘iyyah fī al-Maṣrifiyaah al-Islāmiyyah". p13.

¹⁰⁵² A personal interview with Majed Alrasheed on 12 April 2013, Riyadh Saudi Arabia

speak with SAMA about some issues which these banks are facing. However, even if such guidelines were issued, they would not be enforceable, nor would the committee assess IIFS compliance with them.

Several suggestions have been made to overcome the absence of a framework for Islamic finance in the KSA. The Abdulaziz AlGasim Law Firm has proposed a draft for a law establishing The Committee of Developing Islamic Financial Services (CDIFS).¹⁰⁵³ AlGasim believes that the lack of supervisory authority has achieved an effect in direct opposition to the objectives of Islamic finance.¹⁰⁵⁴ His law firm is not in favour of a centralised SSB, especially in terms of standardising Shari‘ah rulings. It is proposing strong corporate governance rules while leaving Shari‘ah standard-setting to private SSBs.¹⁰⁵⁵ The CDIFS would be overseen by a board of directors consisting of the finance minister, the governor of SAMA, the chief of the Capital Market Authority, its CEO, and three experts in Islamic finance services. The board would coordinate the policies of these authorities towards the development of the Islamic finance industry without overlapping with the powers of the authorities who supervise IIFS. It would act as an advisory body as well as a supervisory one on matters that do not fall under the authority of the three entities.¹⁰⁵⁶

The objectives of establishing CDIFS include organising and promoting Islamic financial services to secure Saudi Arabia’s leadership in the industry,¹⁰⁵⁷ transferring knowhow and expertise from other countries to the Saudi market, improving the efficiency of the industry, and promoting fair dealings, transparency, consumer

¹⁰⁵³ Abdulaziz AlGasim Law Firm, "al-Khadamāt al-Māliyyah al-Islāmiyyah fī al-Mimlakh al-‘arabiyaah al-Su‘ūdiyyah: al-Tanmiyyah wa al- Ḥawkamah," (Riyadh2009).

¹⁰⁵⁴ Ibid., p1.

¹⁰⁵⁵ al-Saud, "Siyāsah al-Jawdah al-Shar‘iyyah fī al-Maṣrifiyaah al-Islāmiyyah". p16.

¹⁰⁵⁶ Abdulaziz AlGasim Law Firm, "al-Khadamāt al-Māliyyah al-Islāmiyyah fī al-Mimlakh al-‘arabiyaah al-Su‘ūdiyyah: al-Tanmiyyah wa al- Ḥawkamah," p46.

¹⁰⁵⁷ Ibid.

protections, and the integrity of the financial system, in addition to enhancing the compatibility of Islamic finance products with the objectives of Shari‘ah.¹⁰⁵⁸

To achieve these objectives, CDIFS would have the power to issue Shari‘ah and accounting best practise standards, raise consumer awareness, review the standards of their protections,¹⁰⁵⁹ promote standardisation, and oversee IIFS compliance with these standards. It also would have power to set the requirements for licences for providing Islamic finance services.¹⁰⁶⁰

Articles 12, 13, 15, and 16 of the proposed law represent further attempts to regulate Shari‘ah governance. Article 12 establishes, by a decision of the council of ministers, an independent association for Shari‘ah supervisory boards which would be under the supervision of CDIFS. The association would set the requirements for practicing Shari‘ah auditing, its code of ethics, and the training and the discipline of SSB members as well as reviewing implementations of the Shari‘ah standard.¹⁰⁶¹

Article 13 of the proposed law imposes a duty on all IIFS to review the Shari‘ah compliance of their products and services through a licensed Shari‘ah auditor. The CDIFS would issue rules regulating the profession of Shari‘ah auditing, which include, *inter alia*, the way of appointing Shari‘ah auditors, auditors’ committee membership requirements, and restrictions on multiple memberships on auditing committees.¹⁰⁶² The rules would also set the requirements for licensing Shari‘ah auditing firms, which would include disclosing Shari‘ah auditing fees and the procedure of Shari‘ah auditing, documenting and publishing SSB rulings, and providing CDIFS with a summary of the principles approved by the firm’s SSB.¹⁰⁶³

¹⁰⁵⁸ Ibid., p47.

¹⁰⁵⁹ Ibid., p48.

¹⁰⁶⁰ Ibid.

¹⁰⁶¹ Ibid., p51.

¹⁰⁶² Ibid.

¹⁰⁶³ Ibid.

Besides this, CDIFS would regulate internal Shari‘ah auditing, its procedures, and the specifications and duration of the auditing reports. IIFS would provide CDIFS and general consumers with a copy of the report of the external Shari‘ah auditor.¹⁰⁶⁴

Article 15 specifically addresses the issue of transparency. It states that CDIFS would issue rules for the transparency of Islamic financial services, which are to be updated regularly. The rules would enforce the duty of documenting and recording the activities and the process of Shari‘ah supervision and auditing, as well as documenting the Shari‘ah principles which are to be made public and to be submitted to CDIFS. The rules would require publication of the principles which the SSBs have approved. CDIFS would also organise a periodic conference where disputed issues would be presented and decided.¹⁰⁶⁵

Article 16 deals with international Islamic financial products offered in the Saudi market. It states that CDIFS would oversee services provided by international IIFS and issue rules regulating the process of approving international Shari‘ah-compliant products and services to the Saudi market in a way that complies with the principles of *fatwa* in Islamic legal theory.¹⁰⁶⁶

The proposed law of CDIFS thus generally deals with most Shari‘ah governance issues. If enacted, it would be a good step in the right direction. It follows an approach that is less centralised than the one applied in Malaysia. However, the enforcing power of CDIFS is not clearly defined; that is, its supervisory function is not distinguished from its advisory function. Besides, since the draft of the CDIFS law was published in 2009, no comments have been made by the regulatory authorities, which suggests that CDIFS is unlikely to be enacted in the near future.

¹⁰⁶⁴ Ibid., p52.

¹⁰⁶⁵ Ibid.

¹⁰⁶⁶ Ibid.

CDIFS is not without its detractors, though. Abdalaziz Ibn Sttam al-Saud criticises the AlGasim firm's proposal, arguing that such an arrangement gives the government too much control over Islamic finance industry.¹⁰⁶⁷ It is inappropriate, he contends, for a governmental department to assess the Shari'ah quality of SSB decisions. Alternatively, Al-Saud suggests establishing a professional non-governmental body that specialises in issuing and reviewing Shari'ah quality standards, called the Saudi Authority for Islamic Financial Standards (SAIFS). The board of SAIFS would consist of a chairman to be appointed by a royal decree, representatives of the relevant governmental bodies, and experts representing professional, financial and economical bodies.¹⁰⁶⁸ It would have a general association of professionals in the relevant area. SAIFS would not have the function of issuing *fatwas* or approving products; its task would be to issue standards which can be used to implement SSB *fatwas* and to properly audit them. In addition, Al-Saud suggests that there should be a body within the Saudi judicial system which can assert Shari'ah standards to add a certainty to these standards and lower their legal risk.¹⁰⁶⁹ He suggests that this task should be conducted by the general committee of the High Court in Saudi. As for issuing *fatwas*, this responsibility should be assigned to a subcommittee of the Council of Senior Ulama, the official body of *fatwas* in Saudi Arabia.¹⁰⁷⁰ Al-Saud's aim seems to be focusing SAIFS's work on Shari'ah quality standards and utilising existing official bodies to undertake other tasks that are usually carried out by the central Shari'ah board in other countries. However, is not clear how Al-Saud categorises SAIFS as a non-governmental body when its chairman is appointed by a royal decree and its board consists of many governmental bodies' representatives. Besides, the structure

¹⁰⁶⁷ al-Saud, "Siyāsah al-Jawdah al-Shar'īyah fī al-Maṣrifīyah al-Islāmiyah". p16.

¹⁰⁶⁸ Ibid., p69.

¹⁰⁶⁹ Ibid., p70.

¹⁰⁷⁰ Ibid., p66.

Al-Saud is proposing assigns many tasks to various bureaucratic state authorities, such as the general committee of the High Court and the Council of Senior Ulama, and this might not suit the needs of the financial industry, which requires speed and flexibility.

Al-Muzaynī,¹⁰⁷¹ a Saudi Shari‘ah scholar, suggests establishing the Supreme Commission for Financial Fatwa (SCFF), an independent self-regulatory body regulating the governance of SSB. The members of SCFF and its head would be yearly elected by representatives of IIFS. The aim of this body, according to al-Muzaynī, would be to ensure stability in the Islamic finance industry, eliminating irregular *fatwas* as well as enhancing the credibility of SSB *fatwas*. It also should aim to protect SSB members’ impartiality and independence and ensure that their *fatwas* are not influenced by pressure from IIFS, the central bank, and the market. The SCFF should not aim to achieve absolute uniformity in *fatwas* or to overlook emergencies and the special circumstances of each IIFS. It should aim for harmonizing *fatwas* and enhancing the ethical aspect of Shari‘ah-compliant products rather than preventing any new *ijthad*.¹⁰⁷²

The tasks of SCFF, according to al-Muzaynī, should include promoting coordination and collaboration¹⁰⁷³ and exchanging Shari‘ah opinions among the SSB members of the SCFF. If there is an inconsistency between SSBs, the matter should be referred to the SCFF, which would issue a binding opinion on it. Only widely used contracts and newly innovated financial products that could shift the industry should be submitted before the SCFF for approval. The SCFF would also issue a report

¹⁰⁷¹al-Muzaynī, "Tarshīd al-‘Amal Fī al-Ha’āt al-Shar‘iyyah Lil-mu’assasāti al-Māliyyah al-Islāmiyyah," p20.

¹⁰⁷² Ibid., p22.

¹⁰⁷³ Ibid., p23.

certifying the procedure for approving Shari‘ah-compliant products in each member SSB.¹⁰⁷⁴

Out of the three suggestions discussed here, al-Muzaynī’s proposal seems most suitable in the short term for the Saudi situation, because the SCFF is a self-regulatory body which does not require the involvement of governmental entities. However, although fully flagged Islamic financial institutions might agree to such proposal, it is unlikely that all Shari‘ah-compliant product providers would comply with SCFF decisions. This could be especially the case for conventional financial institutions offering Islamic windows. Nevertheless, in the long term, a stronger regulatory action is required from the Saudi authorities. Many observers such as Alrasheed¹⁰⁷⁵ believe that SAMA eventually will be forced to regulate the Shari‘ah governance in IIFS.

Establishing a central Shari‘ah board is not the only way to remedy creative Shari‘ah compliance. The next section discusses another public mechanism: enforcing compulsory disclosure by regulators to remedy creative Shari‘ah compliance

6.8. Compulsory Disclosure

One of the remedies which can be used to prevent creative Shari‘ah compliance is increasing the level of disclosure that regulators require of IIFS. This tool can particularly be utilised by regulators in secular countries to increase consumer protection without the need to enact a Shari‘ah governance framework. Consumers should be fully aware of the role and the status of SSBs to be able to make an informed decision. They should be able to trust that an IIFS is a truly Shari‘ah compliant if it presents itself that way.¹⁰⁷⁶

¹⁰⁷⁴ Ibid., p24.

¹⁰⁷⁵ A personal interview with Majed Alrasheed on 12/4/2013., Riyadh Saudi Arabia

¹⁰⁷⁶ Verhoef, Azahaf , and Werner, *Islamic Finance and Supervision: an Exploratory Analysis*, p28.

However, in practise, many IIFS are not transparent with their consumers about what they do to ensure the Shari'ah compliance of their activities.¹⁰⁷⁷ For instance, according to Section 4.4A¹⁰⁷⁸ of the UK Conduct of Business Sourcebook (MCOB),¹⁰⁷⁹ financial institutions which offer home purchase plans (Shari'ah-compliant mortgages) are required by the FCA to provide clients with an Combined Initial Disclosure Document (CIDD).¹⁰⁸⁰ This FCA form is the only document which has a section informing consumers about the product's compliance with Shari'ah. The section asks firms to include the following statement in their CIDD: "Our services are regularly checked by [name(s) of scholar(s)] to ensure compliance with Islamic law. Ask us if you want further information about the role of our scholar(s)".¹⁰⁸¹ However, this requirement is only limited to Islamic financial products under home purchase plans and is not extended to other Shari'ah-compliant products offered in the industry.

To remedy this lack of transparency, regulators should enhance disclosure in two areas: the annual reports of SSBs and the Shari'ah governance of IIFS. To make annual SSB reports more effective, a report issued by the Islamic Finance Council UK (IFC) and the International Shari'ah Research Academy for Islamic Finance (ISRA)¹⁰⁸² suggests that SSBs follow the practise of conventional auditing when describing an institution's Shari'ah compliance. This schema includes four types of auditing opinions, namely, unqualified opinion, qualified opinion, adverse opinion,

¹⁰⁷⁷ Ibid.

¹⁰⁷⁸ Financial Services Authority, "Mortgage Market Review (Conduct Of Business) Instrument 2012," FSA,, http://media.fsahandbook.info/Legislation/2012/2012_46.pdf. accessed 10 May 2013

¹⁰⁷⁹ This section comes into force on 26 April 2014. Prior to that, the requirement is included under 4.4.1R of MCOB.

¹⁰⁸⁰ Financial Conduct Authority (FCA), "Combined Initial Disclosure Document " FCA,, http://www.fca.org.uk/static/fca/documents/handbook/cobs6_annex2_20130401.doc. accessed 1 March 2014

¹⁰⁸¹ Ibid.

¹⁰⁸² Islamic Finance Council UK (IFC) and International Shari'ah Research Academy for Islamic Finance (ISRA), "Enhancing Shari'ah Assurance," IFC,, <http://www.ukifc.com/ifc-isra-launch-pioneering-shariah-assurance-report>. accessed 16 May 2013

and disclaimer.¹⁰⁸³ The unqualified opinion is issued where the auditor deems that a financial statement is fair and accurate and was conducted in line with an appropriate standard of financial reporting. The qualified opinion is where the auditor cannot issue an unqualified opinion, but the discord is substantial enough to require issuing an adverse opinion or a disclaimer. For example, an SSB can issue a qualified opinion if limited incidences of noncompliance with Shari‘ah occurred or if the SSB was not granted full access to product documentation. It also can be used where a product is based on a structure or a contract which is known to be not accepted in certain jurisdictions. For example, a product that is based on *innah* is likely to be rejected by Shari‘ah scholars in GCC countries, but not in Malaysia. The report can include a paragraph clarifying why a qualified opinion has been issued. This kind of disclosure will raise the transparency level of IIFS activities and give peace of mind to international investors. The adverse opinion is issued where the auditor deems the discord substantial and requiring disclosure. Finally, a disclaimer is usually issued where the scope of auditing is substantially limited, to an extent which disables the auditor from reaching an opinion on the financial statements of IIFS due to the lack of evidence.¹⁰⁸⁴

The report also suggests that SSBs use what is known in conventional finance auditing as the Emphasis of Matter paragraph (EMP),¹⁰⁸⁵ where the auditor can draw users’ attention to an important matter presented in the financial statements which he feels is essential to understanding the report. SSBs could include a similar section in their annual report which can be titled Matters of Shari‘ah Emphasis (MSE), where it can raise its concerns over certain issues with regard to the Shari‘ah compliance of an IIFS. For example, an MSE could be used to criticise the heavy use of certain product

¹⁰⁸³ Ibid., p15.

¹⁰⁸⁴ Ibid.

¹⁰⁸⁵ Ibid.

structures by the IIFS which are seen as not in line with the spirit of Islamic law, or it could be used to highlight particular areas which were not adequately addressed by the IIFS management. The possibility of inserting an MSE section within the SSB annual report would put pressure on IIFS management to comply with SSB decisions as well as enabling SSB members to fulfil their duty of care towards stakeholders in a very transparent way. International standard-setting bodies such as AAOIFI and IFSB can help to issue guidelines as to when these recognised opinions and MSEs can be used in SSB annual reports.¹⁰⁸⁶

The annual reports of SSBs could additionally be improved if regulators set further requirements for disclosures in relation to non-Shari'ah income purification.¹⁰⁸⁷ For example, what is the value of the income? How much was purified during the period of the financial statement, and why was the rest not purified? It also should indicate the nature of the charities which benefit from the purification process and their relation to the IIFS. The management should include a statement confirming that the IIFS has not benefited from the money allocated for purification.

Moreover, the IFSB standard on Transparency and Market Discipline (IFSB-4)¹⁰⁸⁸ provides several provisions which can be used to increase the level of Shari'ah compliance in the industry. For instance, it recommends IIFS disclose whether they only offer Shari'ah-compliant services or provide conventional finance with Islamic

¹⁰⁸⁶ Ibid.

¹⁰⁸⁷ Ibid., p23.

¹⁰⁸⁸ Islamic Financial Services Board (IFSB), "Disclosures to Promote Transparency and Market Discipline for Institutions offering Islamic Financial Services," IFSB,, <http://www.ifsb.org/standard/ifsb4.pdf>. accessed 19 May 2013

windows.¹⁰⁸⁹ It also suggests disclosing any losses resulting from non-compliance with Shari'ah.¹⁰⁹⁰

With regard to enhancing disclosure in relation to the Shari'ah governance of IIFS, chapter five mentioned that SSB members' independence can be affected if they have any financial or personal interests in the IIFS.¹⁰⁹¹ The IFC/ISRA recommendations for SSB reports suggest establishing an appropriate mechanism of disclosure to mitigate these risks.¹⁰⁹² Similarly, transparency is also needed for Shari'ah consultancy and auditing firms, particularly in areas related to the governance and management structures of auditing firms, their quality and control systems, policies and procedures with regard to human resource and training, and codes of independence and ethics. Section six of the IFSB Standard on Transparency and Market Discipline is dedicated to Shari'ah governance disclosures of an IIFS in terms of its structure, procedures, and functioning.¹⁰⁹³ IFSB strongly recommends following the approach of "comply or explain". The standard includes the requirements of qualitative and quantitative disclosures shown in Table 4. If this standard were adopted, it would provide a high level of disclosure which would increase transparency within the industry and help consumers to make an informed decision.

¹⁰⁸⁹ Ibid., p6.

¹⁰⁹⁰ Ibid., p22. IFSB define Shari'ah non-compliance risk as "the risk that arises from an IIFS's failure to comply with the Shari'ah rules and principles determined by the Shari'ah Board of the IIFS or the relevant body in the jurisdiction in which the IIFS operate."

¹⁰⁹¹ See: 5.4.5. The Lack of Independence of SSBs; p167

¹⁰⁹² Islamic Finance Council UK (IFC) and International Shari'ah Research Academy for Islamic Finance (ISRA), "Enhancing Shari'ah Assurance" p16.

¹⁰⁹³ Islamic Financial Services Board (IFSB), "IFSB-4" p28.

Table 4. IFSB Shari‘ah Governance Disclosures

| | | |
|--------------------------|--|---|
| Qualitative Disclosures | | A statement on the governance arrangements, systems, and controls employed by the IIFS to ensure Shari‘ah compliance and on how these meet applicable national or international standards. If there is less than full compliance with desirable standards, the reasons for non-compliance should be explained. In countries where national guidelines on Shari‘ah governance in IIFS exist, and the related governance requirements of the IFSB’s Corporate Governance Standard are followed, a statement of compliance with these standards (and reasons for any non-compliance) should be provided. |
| | | Disclosure of how non-Shari‘ah-compliant earnings and expenditures occur and the manner in which they are disposed of. |
| | | Disclosure of whether compliance with Shari‘ah rulings is mandatory or not. |
| Quantitative Disclosures | | Disclosure of the nature, size, and number of violations of Shari‘ah compliance during the year |
| | | Disclosure of annual <i>zakat</i> contributions of the IIFS, where relevant, according to constitution, general assembly, or national requirements. |
| | | Disclosure of remuneration of Shari‘ah board members |

Source: IFSB Standard on Transparency and Market Discipline (IFSB-4)¹⁰⁹⁴

Disclosure in the manners mentioned above can be initiated voluntarily in a sort of self-regulation. Alternatively, standard-setting bodies and national regulators can impose minimum disclosure requirements for SSBs and Shari‘ah auditing firms.¹⁰⁹⁵

6.9. Conclusion

This chapter has suggested two public mechanisms where a national body is involved in remedying the issue of creative Shari‘ah compliance. The first one is to establish a central Shari‘ah supervisory board (CSSB), either as a self-regulatory body or as a unit within the central bank which acts as the authority overseeing the Shari‘ah governance and the implementation of Islamic finance in the financial industry. Two cases of central Shari‘ah boards in Sudan and Malaysia have been shown to offer a better understanding about the nature of CSSBs’ work. In addition, the attitudes of

¹⁰⁹⁴ Ibid.

¹⁰⁹⁵ Islamic Finance Council UK (IFC) and International Shari‘ah Research Academy for Islamic Finance (ISRA), "Enhancing Shari‘ah Assurance" p18.

regulators in the UK and KSA towards Shari‘ah governance and CSSBs have been discussed in detail.

This remedy might not be desirable in some countries, mostly because establishing a central Shari‘ah board is deemed a religious matter that is beyond the legal authority of a secular regulator. Nevertheless, this chapter has argued that making sure that IIFS have an adequate process of ensuring Shari‘ah compliance and that SSBs have a proper corporate governance culture does not conflict with the secular nature of a regulator. Moreover, this chapter has argued that regulators risk breaching their obligation to protect consumers, one of the main objectives of setting up a financial service authority, if they do not regulate Shari‘ah governance and do not try to prevent creative Shari‘ah compliance in IIFS. The current approach followed by the FCA in the UK and SAMA in KSA with regard to Shari‘ah governance is not adequate to protect consumers from creative Shari‘ah compliance. The FCA and SAMA ought to strongly encourage IIFS and other relevant organisations in the UK and Saudi to at least form a self-regulatory body for the Islamic finance industry.

The second public mechanism proposed in this chapter is increasing the level of disclosure required by regulators from IIFS. This tool can particularly be utilised by regulators in secular countries to increase consumer protection without the need to enact a Shari‘ah governance framework. This chapter recommends that regulators enhance disclosure in two areas: the Shari‘ah governance of IIFS and the annual reports of SSBs. In addition, the chapter recommends adopting the IFSB Standard on Transparency and Market Discipline (IFSB-4). It would provide a high level of disclosure which would increase transparency within the industry and help consumers to make informed decisions.

The next chapter suggests several private mechanisms to remedy creative Shari‘ah compliance which can be employed without governmental involvement.

Chapter Seven: Private Mechanisms to Remedy Creative Shari‘ah Compliance

7.1. Introduction

The previous chapter provided public mechanisms to remedy creative Shari‘ah compliance. This chapter suggests potential mechanisms to remedy creative Shari‘ah compliance which can be employed by private actors in the industry without government involvement. These remedies are particularly useful when institutions offering Islamic financial services (IIFS) are operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari‘ah governance.

The first four mechanisms suggested in the chapter are external, meaning they are applied by a third party outside the financial institution, such as a Shari‘ah compliance rating provided by rating agencies. The remainder are internal mechanisms, meaning they can be employed within the financial institution, such as a whistle-blowing policy

The chapter is structured in eight parts, including this introduction. Starting with external mechanisms, Part 7.2 and Part 7.3 examine how Shari‘ah compliance ratings and Shari‘ah indices can be used to reduce creative Shari‘ah compliance. Part 7.4 highlights the threat of self-review and examines what role private Shari‘ah auditing firms can play in countering this threat. Part 7.5 suggests the adoption of international standards related to enhancing Shari‘ah compliance. Moving to the internal mechanisms, Part 7.6 suggests the adoption of a whistle-blowing policy for serious Shari‘ah-compliance violations. Part 7.7 advocates characterising an IFI in its articles of association as an entity that fully complies with Shari‘ah ruling. Finally, Part 7.8 concludes the chapter.

7.2. Shari‘ah Compliance Rating

One of the external tools to secure Shari‘ah compliance is the use of rating agencies to rate the Shari‘ah compliance of an IIFS or a product with the objectives of Islamic law. The Islamic International Rating Agency (IIRA) was one of the first rating agencies to issue a rating based on the Shari‘ah compliance.¹⁰⁹⁶ IIRA was established in 2005 by shareholders from eleven countries, including multilateral development institutions, top banks, and other financial institutions and rating agencies. Grais and Pellegrini¹⁰⁹⁷ suggest that private rating agencies have not acquired the expertise or seen sufficient incentives to conduct a Shari‘ah compliance rating. Therefore, the task remains with ultimately government-sponsored institutions such as the IIRA. Although the primary focus of IIRA is to provide a credit rating for IIFS,¹⁰⁹⁸ it offers other specialised ratings such as corporate governance ratings, fiduciary ratings, and Shari‘ah quality ratings. The latter focus is the one relevant to this chapter’s discussion.

In its methodology for Shari‘ah quality ratings,¹⁰⁹⁹ IIRA states that it aims to offer investors an independent evaluation of the Shari‘ah compliance of either IIFS or Islamic finance products such as *Ṣukūk*. IIRA’s goal is to become a reliable reference in the market for those who seek quality with regard to Shari‘ah compliance. One advantage of the existence of Shari‘ah compliance ratings as a tool is that it could create an environment where IIFS would compete to achieve the highest rating, which

¹⁰⁹⁶Islamic International Rating Agency (IIRA), "Corporate Profile," IIRA, <http://www.iirating.com/CoperateProfile.aspx>. accessed 10 May 2013

¹⁰⁹⁷ Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". p17.

¹⁰⁹⁸Islamic International Rating Agency (IIRA), "Rating," IIRA, <http://www.iirating.com/RatingNavigations.aspx>. accessed 13 May 2013

¹⁰⁹⁹ "Methodology for Shari‘ah Quality Rating," IIRA, http://www.iirating.com/Documents/ResearchReports/sharia_methd_eng.pdf. accessed 10 May 2013

in turn would increase the level of Shari‘ah compliance in the Islamic finance industry as a whole.¹¹⁰⁰

The Shari‘ah quality rating is conducted by specialists overseen by a board of Shari‘ah scholars.¹¹⁰¹ For a rating assignment, a team of three scholars who have no relation with the audited entity are selected by the secretariat of the Shari‘ah Board, which will review the finding of the rating specialists. IIRA management offers technical support to the board and helps to obtain the required information for the rating from the IIFS, including its product structure, related *fatwas*, and the financial statements of the last five years.

When describing its methodology,¹¹⁰² IIRA states that it strives to provide its services to investors following different sects and schools of thought, and therefore it does not seek to issue a *fatwa* or comment on the decision of SSBs. Rather, IIRA’s main task is to assess an IIFS’s compliance with decisions issued by its Shari‘ah supervisory board. However, IIRA made it clear that this does not mean that its Shari‘ah board will not thoroughly review decisions issued by an SSB of an IIFS. IIRA will objectively evaluate any reservations on some *fatwa* expressed by other Shari‘ah scholars. Besides this, IIRA’s assessment will take into account the power and the resources available to an SSB to do its task.¹¹⁰³ For example, it might consider whether an IIFS has internal mechanisms for ensuring Shari‘ah compliance, such as a Shari‘ah unit to review its compliance with the decisions issued by its SSB as well as how it deals with non-Shari‘ah-compliant income.¹¹⁰⁴

IIRA’s methodology also involves examining the structure of assets and liabilities in a product, the IIFS process of Shari‘ah authentication of a product, and the

¹¹⁰⁰ Ibid.

¹¹⁰¹ Ibid., p2.

¹¹⁰² Ibid.

¹¹⁰³ Ibid.

¹¹⁰⁴ Ibid., p3.

credibility and the independence of SSB members who approve a product.¹¹⁰⁵ The Shari'ah quality rating is further influenced by other factors such as the IIFS's disclosure of business activities to its clients, the disclosure of its profit and loss calculation method, the Shari'ah compliance of its ethics code, and its compliance with international standards in Islamic finance such as the Shari'ah standards of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).¹¹⁰⁶ When rating Islamic windows offered by conventional financial institutions, IIRA reviews the procedures taken to ensure that Shari'ah-compliant and conventional funds are not commingled.¹¹⁰⁷

As can be seen in table (3), which shows the process of Shari'ah quality rating, the assessment process is only conducted upon IIFS request.¹¹⁰⁸ The result will not be made public before the approval of the IIFS, which can discuss and appeal the result of the rating. IIRA states that it takes this route because it does not want to have a negative impact on the Islamic finance industry. The rating is valid for one year, during which time IIRA watches and gathers information from the rated IIFS. The rating result might be modified subject to information collected during this year. In case an IIFS chooses not to renew its agreement, its IIRA rating will be publicly withdrawn.

However, a Shari'ah compliance rating as described in the IIRA methodology is unlikely to improve the level of Shari'ah compliance in the industry, as is advocated in this chapter, because IIRA only conducts Shari'ah compliance rating at the request of an IIFS and does not publish the result without IIFS permission. This means that

¹¹⁰⁵ Ibid.

¹¹⁰⁶ Ibid.

¹¹⁰⁷ Ibid. Other factors have been stated in the IIRA methodology of Shari'ah quality rating, but they are not directly related to Shari'ah compliance. For example, the IIRA reviews IIFS accounting policies and practises and its presentation of financial statements as well as its compliance with International Financial Reporting Standards (IFRS).

¹¹⁰⁸ Ibid.

only good ratings will be published, as no IIFS would agree to publish a negative rating. As mentioned, IIRA seeks the approval of an IIFS before rating its Shari'ah compliance because IIRA does not want to have any negative impact on the industry. This stance may suggest that IIRA aims to promote IIFS business rather than increasing the compliance level and protecting consumers. This assumption is further supported by the fact that at the time this chapter was written, all seven IIFS rated by IIRA have been given the second-highest rating possible (AA; see Table 4 for rating definitions).¹¹⁰⁹ IIRA and other rating agencies should conduct unsolicited Shari'ah compliance ratings based on the information disclosed by IIFS, as is the case in credit ratings.¹¹¹⁰ This would encourage IIFS to disclose more information about their Shari'ah-compliant products and Shari'ah governance structure, and generally increase the level of Shari'ah compliance in the industry.

Another issue with the IIRA Shari'ah quality rating is the names of scholars on its Shari'ah supervisory board.¹¹¹¹ The name list shows the presence of many scholars who are among the top Shari'ah scholars in terms of multiple board membership in IIFS.¹¹¹² This cast doubt on the independence of the IIRA Shari'ah quality rating. Besides, some of these Shari'ah scholars have been responsible for authorising some of the most conventional structures in the Islamic finance market, such as organised

¹¹⁰⁹ "Press Releases," IIRA, <http://www.iirating.com/ResourceCenterNavigation.aspx>. accessed 12 May 2013. Only two withdrawals have been announced, one of them because of reasons related to Shari'ah compliance (i.e., the resignation of two senior management persons from the Shari'ah compliance department). See: "IIRA withdraws AA (SQR) rating assigned to Syarikat Takaful Malaysia Berhad " IIRA, http://www.iirating.com/Documents/PressReleasePdf/SQR_withdrawal_of_Syarikat_TM.pdf. accessed 11 May 2013.

¹¹¹⁰ Financial Times Lexicon, "Unsolicited Rating," Financial Times,, <http://lexicon.ft.com/Term?term=unsolicited-rating>. accessed 18 May 2013; Winnie P. H. Chan Kam C. Poon, "Solicited and Unsolicited Credit Ratings : a Global Perspective," Asian Development Bank Inst., <http://www.adbi.org/working-paper/2010/08/24/4048.solicited.unsolicited.credit.ratings.global/>. accessed 11 May 2013

¹¹¹¹ Islamic International Rating Agency (IIRA), "Methodology for Shari'ah Quality Rating" p6.

¹¹¹² Compare it with the names in Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

tawarruq.¹¹¹³ For example, Sheikh Nizam Yaquby has publicly challenged the International Fiqh Academy Council prohibition on organised *tawarruq*.¹¹¹⁴ Even if the subcommittee selected by the IIRA SSB to rate an IIFS has no direct relation with that IIFS, it would be difficult for scholars to be objective about the performance of an SSB that is headed by their colleague in the Shari‘ah supervisory board of IIRA. This might be especially the case taking into account the high religious status which Shari‘ah scholars usually enjoy in their societies. This situation poses a serious question about conflicts of interest in the IIRA Shari‘ah board, and whether IIRA is able to achieve its primary task with its current SSB members.

For the Shari‘ah compliance rating to help increase the level of compliance in the industry, it should be carried out by more independent rating agencies, and a higher weight should be given to the substance of products in the results of the rating. Some credit rating agencies such as Moody have expressed concern over the substance of some products and their non-Shari‘ah-compliance risk, which might have an impact on the credit profile of an IIFS.¹¹¹⁵ Prominent credit rating agencies might do well to employ Shari‘ah experts and extend their services to include Shari‘ah compliance rating. With the industry expanding, Shari‘ah compliance ratings will be necessary to prevent the spread of creative Shari‘ah compliance practises.

¹¹¹³ See: Mohammed Khnifer, "Ya‘qūbī li "ālāqtiṣādiyah": Lam Atahadda Majma‘ al-Fiqh Bifatwā al-Tawarq wa‘alā al-Fuqahā’ al-Tafrīq bana «al-Munḍabiṭ» wa«ghari al-Munḍabiṭ»", *Alaqtadyh*, 52/07/2010 http://www.aleqt.com/2010/07/25/article_422297.html. accessed 11 May 2013; Muḥammad al-Hamazānī, "Ra’īs Ha’ah Shar’iyyah fī Akbar Bank Islāmī Uḥarim al-Tawaruq wa Uaṣifuh bi al-Ribā al-Mastūr", *Asharq Al-Awsat*, 14/9/2010 <http://www.aawsat.com/details.asp?issueno=11700&article=586625#.UeYQQNLI4VR>. accessed 10 May 2010

¹¹¹⁴ Khnifer, "Ya‘qūbī li "ālāqtiṣādiyah": Lam Atahadda Majma‘ al-Fiqh Bifatwā al-Tawarq wa‘alā al-Fuqahā’ al-Tafrīq bana «al-Munḍabiṭ» wa«ghari al-Munḍabiṭ»."; al-Hamazānī, "Ra’īs Ha’ah Shar’iyyah fī Akbar Bank Islāmī Uḥarim al-Tawaruq wa Uaṣifuh bi al-Ribā al-Mastūr."

¹¹¹⁵ See for example: Howladar, "The Future of Sukuk: Substance over Form?"; "Shari‘ah Risk: Understanding Recent Compliance Issues in Islamic Finance".

Table 5. Shari‘ah Quality Rating

| | | |
|-----------------------------------|----|---|
| Issuer/Client | 1 | Signs agreement for rating with IIRA |
| | 2 | Submits preliminary information materials to IIRA |
| IIRA | 3 | Tells the Secretariat of the Shari‘ah Board to formulate the Shari‘ah Quality Rating Committee |
| | 4 | Conducts a preliminary study and sends the preliminary information to the Shari‘ah Quality Rating Committee |
| Shari‘ah Quality Rating Committee | 5 | Liaises with IIRA to submit a detailed questionnaire to the issuer/client |
| Issuer/Client | 6 | Provides detailed information in response to detailed questionnaire |
| IIRA | 7 | Establishes with the Shari‘ah Quality Rating Committee the points to be covered during due diligence |
| | 8 | Conducts pre–due diligence meeting analysis |
| | 9 | Conducts due diligence meetings |
| | 10 | Conducts post–due diligence analysis |
| | 11 | Submits report to Shari‘ah Quality Rating Committee |
| Shari‘ah Quality Rating Committee | 12 | Decides the preliminary/initial rating |
| IIRA | 13 | Notifies issuer/client of the preliminary/initial rating |
| | 14 | Discusses the rating rationales and issues with issuer/client |
| Issuer/Client | 15 | May appeal based on any new facts or information |
| Shari‘ah Quality Rating Committee | 16 | Deliberates on appeals by issuer/client and gives decision |
| IIRA | 17 | Communicates the decision of the Shari‘ah Quality Rating Committee to the issuer/client |
| Issuer/Client | 18 | Consents to release of the rating to the public |
| IIRA | 19 | Releases the rating to media |

Table 6. IIRA Rating

| | |
|-----------|---|
| AAA (SQR) | In IIRA's opinion, an entity/instrument rated AAA (SQR) conforms to highest level of standards of Shari'a requirements in all aspects of Shari'a quality analysis |
| AA(SQR) | In IIRA's opinion, an entity/instrument rated AA (SQR) conforms to very high level of standards of Shari'a requirements in all aspects of Shari'a quality analysis |
| A(SQR) | In IIRA's opinion, an entity/instrument rated A (SQR) conforms to high level of standards of Shari'a requirements and has very few weaknesses in some areas of Shari'a quality analysis |
| BBB(SQR) | In IIRA's opinion, an entity/instrument rated BBB (SQR) conforms to moderately high level of standards of Shari'a requirements and has few weaknesses in some areas of Shari'a quality analysis |
| BB(SQR) | In IIRA's opinion, an entity/instrument rated BB (SQR) conforms to satisfactory level of standards of Shari'a requirements and has some weaknesses in some areas of Shari'a quality analysis |
| B(SQR) | In IIRA's opinion, an entity/instrument rated B (SQR) conforms to adequate level of standards of Shari'a requirements and has weaknesses in some areas of Shari'a quality analysis |

Source: IIRA, "Methodology for Shari'ah Quality Rating"

7.3. Shari‘ah Indices

Shari‘ah indices are a second tool that can be used to increase the level of Shari‘ah compliance. These indices were initially developed for Shari‘ah-compliant investment in stock markets. They can be issued individually by Shari‘ah scholars or in a more organised way by financial institutions such as credit rating agencies. One of the first attempts to create a Shari‘ah-compliant index was the Dow Jones Islamic Market Index (DJIMI),¹¹¹⁶ which was established in 1999 in Bahrain to help Muslim investors who wanted to invest in the Dow Jones stock market. It has now issued a family of indices in at least 69 countries. The DJIMI has its own Shari‘ah supervisory board, which has an advisory role and submits recommendations to the DJIMI steering committee, which in turn has the power to issue final business decisions.¹¹¹⁷ Currently, there are several Shari‘ah-compliant indices issued by various companies, including Standard & Poor’s, the Russell-Jadwa Shari‘ah Index,¹¹¹⁸ Thomson Reuters Islamic Indices, and FTSE Shari‘ah Global Shari‘ah Global Equity Index.¹¹¹⁹ Besides these, several Shari‘ah scholars have issued unofficial Shari‘ah indices in addition to the percentages of non-Shari‘ah income which investors need to purify by paying it to charity.¹¹²⁰

The basic methodologies for calculating these indices are generally based on the business activities and the debt structure of the listed companies. The index first

¹¹¹⁶ M. Fahim Khan and Mario Porzio, *Islamic Banking and Finance in the European Union: A Challenge* (Edward Elgar Ltd, 2010), p137.

¹¹¹⁷ CME Group Index Services, "Guide to the Dow Jones Islamic Market Indexes," CME Group Index Services, accessed 15 May 2013

¹¹¹⁸ Jadwa, "Launch of the Russell-Jadwa Shariah Indexes," Jadwa <http://www.jadwa.com/en/news/news/news-2009/launch-of-the-russell-jadwa-shariah-indexes.html>. accessed 22 May 2013

¹¹¹⁹ FTSE Group, "FTSE Shariah Global Equity Index Series," FTSE, http://www.ftse.co.uk/Indices/FTSE_Shariah_Global_Equity_Index_Series/index.jsp. accessed 22 May 2013

¹¹²⁰ ‘Abdāl’ azīz al-Fūzān, "Qā’imah al-Ashum al-Mubāḥah," The message of Islam <http://main.islammessage.com/newspage.aspx?id=9663>. accessed 28 May 2013; Yūsuf ‘AbdAllāh al-Shabīlī, "Qā’imah al-Ashum al-Jā’izah " Shubily, <http://www.shubily.com/index.php?news=348>. accessed 10 May 2013

excludes any company that engages in prohibited and harmful activities, such as the manufacturing of alcohol, pork-related products, entertainment, tobacco, and conventional financial services.¹¹²¹ Listed companies then are screened to assess their capital structure. Their debt level should be less than 33% of company capital.

These Islamic financial indices help to increase the general level of Shari'ah compliance in some Muslim countries such as Saudi in the sense that they encourage companies to use Shari'ah-compliant financing methods rather than conventional ones. However, they are not sufficient to deal with the issue of creative Shari'ah compliance or to substitute for the role of Shari'ah compliance rating agencies, because Islamic indices are limited to the capital market, which tends to attract certain types of investors. It does not include other Shari'ah-compliant products which usually are used by general consumers.

In addition, the methodology of composing Shari'ah-compliant indices is fairly controversial among Shari'ah scholars.¹¹²² For example, there is no agreement regarding the accepted level of debt or the percentage of non-halal income of a company to be included in Shari'ah-compliant indices.¹¹²³ Also, should the calculation of the debt structure be based on the book value or the market value of the company?¹¹²⁴ There is also the question of whether financial statements represent a reliable account for screening non-Shari'ah-compliant liability and assets. In short, neither Islamic indices nor Shari'ah compliance ratings as currently practised by IIRA represent the desired form of Shari'ah compliance rating.

¹¹²¹ The DJIMI SSB does not allow investing in companies involved in these activities where impure sources exceed 5% of their revenue. See CME Group Index Services, "Guide to the Dow Jones Islamic Market Indexes" p5.

¹¹²² See Grais and Pellegrini, "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services". p17.

¹¹²³ Ibrāhīm al-Sakrān, *al-Ashum al-Mukhtalīṭah* (Wahaj al-ḥayāh Lil-'lām, 2005); ṣāliḥ al-'Iṣaymī, *al-Ashum al-Mukhtalīṭah fī Mīzān al-Sharī'h* (al-Tadmuriyyah, 2008).

¹¹²⁴ Abdul-Rahman, *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*, p365.

7.4. Private External Shari‘ah Auditing Firms

One of the remedies which can help to strengthen Shari‘ah compliance in the IIFS are the use of private Shari‘ah auditing firms (SAFs), or Shari‘ah consulting firms (SCFs),¹¹²⁵ as they can be called sometimes, to mitigate the risk of self-review. IIFS tend to employ an SSB to ensure the Shari‘ah compliance of its business activities. The tasks of the SSB usually consist of structuring Shari‘ah-compliant products (*ex ante* review), and also verifying that implementations of these structures are in line with Shari‘ah (*ex post* review).¹¹²⁶ The objectivity and the independence of the SSB are endangered since Shari‘ah scholars have two roles: structuring the product and ensuring its compliance. This leads to what is known as a “self-review threat”.¹¹²⁷ A report issued by the Islamic Finance Council UK (IFC) and the International Shari‘ah Research Academy for Islamic Finance (ISRA)¹¹²⁸ suggests following the guidelines of auditing in the conventional market where auditing firms might be restricted from providing advisory services and auditing the same work on which they had consulted.¹¹²⁹ Accordingly, the task of designing and approving Shari‘ah-compliant products should be separated from the task of ensuring their compliance.¹¹³⁰

The first SAF emerged in 2003 in Kuwait, and others have been subsequently established in the remaining GCC countries in the addition to the UK.¹¹³¹ The

¹¹²⁵ See: Abdulbari Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyāt " (paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, 27 - 28/5/2008).

¹¹²⁶ Islamic Finance Council UK (IFC) and International Shari‘ah Research Academy for Islamic Finance (ISRA), "Enhancing Shari‘ah Assurance" p10.

¹¹²⁷ Ibid.

¹¹²⁸ Ibid., p11.

¹¹²⁹ See: The Auditing Practices Board, "APB Ethical Standard 5: Non-Audit Services Provided To Audited Entities " Financial Reporting Council (FRC),, [https://www.frc.org.uk/Our-Work/Publications/APB/ES-5-\(Revised\)-Non-audit-services-provided-to-\(2\).pdf](https://www.frc.org.uk/Our-Work/Publications/APB/ES-5-(Revised)-Non-audit-services-provided-to-(2).pdf). accessed 1 March 2014

¹¹³⁰ Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyāt " p8.

¹¹³¹ ‘Abd al-Sattār al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt" (paper presented at the The 8th Conference of Shari‘a Supervisory Boards of Islamic

emergence of these firms has been attributed by some researchers to the fact that some SSB tend to take a long time to approve the compliance of IIFS products and transactions, due to the shortage of Shari‘ah scholars, among other reasons. This might have caused IIFS to miss some investment opportunities which cannot tolerate such delay. Therefore, IIFS have been motivated to assign the task of SSBs to private Shari‘ah auditing firms, which can provide the service at a lower cost and in a more efficient way because of its specialized and full-time staff.¹¹³² There is no standard legal framework for SAFs. While some of them are authorised by central banks, as in Kuwait and Bahrain,¹¹³³ others are only registered as companies with the ministry of commerce.¹¹³⁴

SAFs offer several services to their clients.¹¹³⁵ For example, they can function as an SSB of an IIFS, with the Shari‘ah board members of the SAF acting as the SSB members of the IIFS. In this position, they can provide an *ex ante* and *ex post* Shari‘ah review. The SAF would carry out its meeting preparation and any secretarial work that is usually done by an internal SSB. This service is the most popular one of SFAs, and it is commonly used by new IIFS. SAFs can also provide external Shari‘ah review and report back to the SSB or to the management of the IIFS. The review can be conducted to examine the compliance of an IIFS with the decisions of its SSB.

Financial Institutions, Bahrain, 18-19/5/2009), p4. According to al-Qaṭṭān, at least there are 20 SAF in GCC and 8 in Kuwait.

¹¹³²Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p3; al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt," p5.

¹¹³³See for example: Shariyah Review Bureau, "About Us," Shariyah Review Bureau,, http://www.shariyah.com/?page_id=15. accessed 18 May 2013. Some SAFs in the UK are regulated by FSA; see: Simply Sharia, "About " Simply Sharia,, <http://www.simplysharia.com/About/1/>. accessed 14 May 2013

¹¹³⁴ al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt," p8; Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p4.

¹¹³⁵"Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p4; al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt," p6; Shura Sharia Consultancy, "Home," Shura,, <http://www.shura.com.kw/home/pages/default.aspx>. accessed 18 May 2013

However, Mashal¹¹³⁶ notes that SFAs have not been successful in marketing this service. Its credibility and professional integrity have not reached a level which gains the trust of SSBs. Besides, SSBs have yet to realise the importance of auditor independence and the danger of self-review.

Another service that SAFs offer is supervising the conversion of a conventional financial institution into an Islamic financial institution. SAFs can offer alternative Shari‘ah-compliant procedures and product structures.¹¹³⁷ In addition, SAFs can be hired by an IIFS to develop Shari‘ah-compliant products or services. However, some SAFs have not realised that a task like this requires a highly skilled, multidisciplinary team, which might explain why conventional finance consulting firms have attracted more clients for such tasks (e.g., developing *sukūk* structure) though they are not specialists in Islamic finance.¹¹³⁸ Other services offered by SAFs are calculating IIFS’s *zakāh*, developing Shari‘ah-compliant indices, organising workshops and training programmes,¹¹³⁹ and acting as mediators in disputes between IIFS.¹¹⁴⁰

However, it is doubtful that SAFs in their current situation will do much to improve the industry’s level of Shari‘ah compliance. This is because SAFs lack the legal framework for their activities, a situation which has resulted in a few unprofessional governance practises.¹¹⁴¹ For example, there is a question about the independence of SAFs’ Shari‘ah supervisory boards,¹¹⁴² as some SAFs are owned by

¹¹³⁶ Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p4.

¹¹³⁷ Ibid., p6.

¹¹³⁸ Ibid., p7.

¹¹³⁹ Ibid.; al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-āusus wa al-ḍawābiṭ w al-mutaṭallabāt," p4.

¹¹⁴⁰ "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-āusus wa al-ḍawābiṭ w al-mutaṭallabāt," p6.

¹¹⁴¹ Ibid., p8.

¹¹⁴² Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p7.

IIFS, law firms, and Shari‘ah scholars.¹¹⁴³ In addition, the absence of a professional standard for SAFs leads to many conflicts of interest. For example, an SAF might have other financial interests with the audited IIFS, such as conference sponsorships. Mohamad Nedal Alchaar, the Secretary-General of AAOIFI in 2010, expressed the organisation’s concern over some SAFs owned by Shari‘ah scholars receiving favoured treatment from IIFS. In particular, concerns have been raised over potential cases of conflict of interest, breach of confidentiality, and the impact of competition between SAFs.¹¹⁴⁴ Besides, some SAFs agree to only provide a *fatwa* service to IIFS without an *ex post* review of the actual implementation of this *fatwa* in these institutions. Consumers might be misled by the impression that the Shari‘ah compliance of IIFS activities is regularly checked by this specialist SAF. In some cases, an SAF provides *ex ante* and *ex post* Shari‘ah review to one IIFS, which leads to the danger of self-review. Like SSBs, SFAs should not combine the service of product development with the *ex post* Shari‘ah review.¹¹⁴⁵ To avoid this issue, Mashal and other researchers¹¹⁴⁶ suggest a framework where *ex ante* and *ex post* Shari‘ah review are performed by separate auditors. The *ex ante* Shari‘ah review would ideally be provided by an IIFS’s own SSB, while the *ex post* Shari‘ah auditing is performed by an SAF, thereby avoiding the threat of self-review.¹¹⁴⁷

Moreover, it is worth noting that SAF decisions are not binding on IIFS.¹¹⁴⁸ Therefore, Shari‘ah compliance might be questioned if an SAF is acting as the SSB of a bank. An IIFS might not want to restrict itself to one SSB since using an SAF’s

¹¹⁴³ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p85; Dar, "Implementing Shari'ah Governance -Aawaiting Challenges."

¹¹⁴⁴ El Baltaji and Anwar, "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance".

¹¹⁴⁵ Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyāt " p14.

¹¹⁴⁶ Ibid., p8.

¹¹⁴⁷ Ibid.

¹¹⁴⁸ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p86.

fatwa services can offer more flexibility for product approval. This may explain why SAFs are widely used by conventional institutions offering Islamic windows.¹¹⁴⁹ This brings into play the issue of “*fatwa* shopping”, where IIFS search the market seeking approval for a particular product.¹¹⁵⁰ In this sense, SAFs contribute negatively to Shari‘ah compliance and actually facilitate the practise of creative Shari‘ah compliance.

In addition, some SAFs provide services which are beyond their speciality, for example, marketing initial public offerings (IPO),¹¹⁵¹ translating contracts, evaluating SSB staff, and assessing the economic feasibility of Shari‘ah-compliant products. Providing such services distract SAFs from their original task of Shari‘ah compliance auditing and call into question their credibility.¹¹⁵²

To solve these issues, regulators need to consider a legal framework establishing a supervisory body,¹¹⁵³ preferably a self-regulated one,¹¹⁵⁴ to license and oversee SFA conduct, ensure compulsory reporting, and preserve confidentiality and transparency.¹¹⁵⁵ This framework should help to define the scope and the procedures of SAF services, and how its work is different from that of SSBs, internal Shari‘ah auditors, and external financial auditors. The programme of Certified Shari‘ah Adviser and Auditor (CSAA),¹¹⁵⁶ established by AAOIFI, is a good step in

¹¹⁴⁹ Ibid., p319; Dar, "Implementing Shari'ah Governance -Aawaiting Challenges."

¹¹⁵⁰ Dar, "Implementing Shari'ah Governance -Aawaiting Challenges."

¹¹⁵¹ Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p8; al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-āusus wa al-ḍawābiṭ w al-mutaṭallabāt," p7.

¹¹⁵² "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-āusus wa al-ḍawābiṭ w al-mutaṭallabāt," p8.

¹¹⁵³ Mashal, "Sharikāt al-Āsitishārāt al-Shar‘iyyah wa Hay’āt al-Raqābah al-Shar‘iyyah: al-ḍawābiṭ wāl’āliyyāt " p13 & p16.

¹¹⁵⁴ al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-āusus wa al-ḍawābiṭ w al-mutaṭallabāt," p13.

¹¹⁵⁵ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p319.

¹¹⁵⁶ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Certified Islamic Professional Accountants (CIPA)," AAOIFI, <http://www.aoofi.com/aoofi/ProfessionalDevelopment/CertifiedIslamicProfessionalAccountantCIPA/abid/76/language/en-US/Default.aspx>. accessed 14 May 2013

recognising external Shari'ah auditing as a profession. AAOIFI¹¹⁵⁷ also has issued a code of ethics for accountants and auditors of Islamic financial institutions which can be adopted by SAFs.¹¹⁵⁸

7.5. International Islamic Financial Standards

International regulatory and standard-setting bodies are among the main players in the Islamic finance industry which could have an impact on Shari'ah compliance. In particular, two international bodies have been actively engaged with the Islamic finance industry.¹¹⁵⁹ Those are the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB). The former's standards are more directed towards individual IIFS, while the latter's standards are more focused on national regulators.¹¹⁶⁰

AAOIFI is an independent international non-profit corporation established in 1990 in Algiers and registered almost a year later in the Kingdom of Bahrain.¹¹⁶¹ AAOIFI mainly issues Shari'ah, accounting, auditing, governance, and ethics standards for IIFS. It is supported by more than 200 institutional members from 45 countries. AAOIFI standards generally enjoy a good degree of recognition, and its pronouncements have an impact on the market.¹¹⁶² They have been adopted by

¹¹⁵⁷ "AAOIFI Key Publications," AAOIFI, <http://www.aoofi.com/aoofi/Publications/KeyPublications/tabid/88/language/en-US/Default.aspx>, accessed 23 May 2013

¹¹⁵⁸ al-Qaṭṭān, "Sharikāt al-Āsitishārāt al-Shar'iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt," p14; Mashal, "Sharikāt al-Āsitishārāt al-Shar'iyyah wa Hay'āt al-Raqābah al-Shar'iyyah: al-dawābiṭ wāl'āliyyāt " p9.

¹¹⁵⁹ Andrew Henderson, "Islamic Financial Institutions," in *Islamic Finance: Law and Practice*, ed. Craig Nethercott and David Eisenberg (Oxford Oxford University Press, 2012), p57

¹¹⁶⁰ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p86.

¹¹⁶¹ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Overview," AAOIFI, <http://www.aoofi.com/aoofi/TheOrganization/Overview/tabid/62/language/en-US/Default.aspx>, accessed 18 May 2013

¹¹⁶² For example, see the impact of AAOIFI Statement on *sukūk* market in: Farmida Bi, "AAOIFI Statement on Sukuk and its Implications," Norton Rose Fulbright, <http://www.nortonrosefulbright.com/knowledge/publications/16852/aoofi-statement-on-sukuk-and-its-implications>, accessed 20 May 2013

various countries including Bahrain, Qatar, Jordan, Lebanon, Sudan, and Syria and other international financial centres such as Dubai International Financial Centre and Qatar Financial Centre. As well, regulatory authorities in other countries, including Malaysia, Pakistan, Australia, South Africa, and Indonesia, have issued guidelines which are based on AAOIFI's standards and decisions.¹¹⁶³ At the time of writing this chapter, AAOIFI published 48 Shari'ah Standards, 23 Accounting Standards, 5 Auditing Standards, 6 Governance Standards, and 2 Codes of Ethics.¹¹⁶⁴

However, concerns have been raised about the regulatory independence of AAOIFI.¹¹⁶⁵ A recent study by Ünal showed that the 12 most active scholars in AAOIFI dominate 38.9% of the available boards in Islamic finance institutions. Moreover, they collectively hold 71.17% of the positions in standard-setting organizations, governmental units, and consulting companies.¹¹⁶⁶ To put it plainly, how can we be assured that standards and frameworks introduced by this entity follow public interests and are not affected by regulatory capture?¹¹⁶⁷ Accordingly, it is no wonder that AAOIFI has so far failed to clearly address the issue of multiple board membership and that its scholars have always voiced their objection to strict governance reforms.¹¹⁶⁸

The Islamic Financial Services Board (IFSB) was established in Kuala Lumpur in 2002 and launched its operations in 2003. It functions as an international standard-setting body of regulatory and supervisory authorities which have an interest in

¹¹⁶³ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Overview".

¹¹⁶⁴ "AAOIFI Key Publications".

¹¹⁶⁵ Alsayed, "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance"; Alkhamees, "The Impact of Shari'ah Governance Practices on Shari'ah Compliance in Contemporary Islamic Finance," p153.

¹¹⁶⁶ Ünal "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective".

¹¹⁶⁷ Regulatory capture occurs when a regulatory body, created to protect the public's interest, ultimately takes action benefitting the industry which it is assumed to be regulating rather than the public. See: Dal Bó, "Regulatory Capture: A Review".

¹¹⁶⁸ See: Richter, "Top Islamic Finance Scholars Oppose Reform Effort".

developing a sound and stable financial market. IFSB aims to develop a prudent and transparent Islamic financial industry by issuing or amending existing international standards to be compatible with Islamic law and recommending their implementation. In this regard, IFSB supplements and builds on the work of the Basel Committee on Banking Supervision, the International Organisation of Securities Commissions, and the International Association of Insurance Supervisors. By the end of 2012, IFSB had 184 members, among them 55 regulatory and supervisory bodies, eight global intergovernmental organisations, and 121 market players working in 41 countries.¹¹⁶⁹ Since its launch, the IFSB has issued 19 Standards, Guiding Principles, and Technical Notes for the Islamic financial industry. Most of these standards are within the domain of prudential regulation, capital adequacy, and risk management.¹¹⁷⁰ Four standards are relevant to the discussion of this chapter: the Guiding Principles on Shari‘ah Governance Systems (IFSB-10), Conduct of Business for Institutions Offering Islamic Financial Services (IFSB-9), Corporate Governance (IFSB-3), and Transparency and Market Discipline (IFSB-4). The standard most interrelated with the issue of Shari‘ah compliance is the first one (IFSB-10). The paragraphs below offer some details of this standard.

The IFSB Guiding Principles on Shari‘ah Governance Systems unsurprisingly shares a core similarity with the Shari‘ah Governance Framework issue by Bank Negara Malaysia (BNM) discussed in chapter six. The standard begins by defining the Shari‘ah governance system and its scope. Section I then sets out the IFSB’s general approach to the Shari‘ah governance system. It lays out *ex ante* steps that should be taken into account at the stage of designing and developing the product, as well as *ex*

¹¹⁶⁹Islamic Financial Services Board (IFSB), "Background," IFSB, <http://www.ifsb.org/background.php>. accessed 20 May 2013

¹¹⁷⁰ Ibid.

post considerations after offering it to consumers.¹¹⁷¹ These *ex ante* and *ex post* procedures are deemed as crucial aspects of good governance practises in various globally recognised governance standards. They include defined terms of reference for the mandate and obligations of SSB members, a clear operating procedure and lines of reporting, and the implementation of a code of professional ethics.

Part II deals with the issue of SSB competence. It introduces several procedures to make sure that only qualified and skilled members are appointed to the Shari‘ah board, and that their proficiency and professional development are continuously assessed. Part III focuses on protecting SSB independence, especially from IIFS management. It underlines different issues resulting from potential conflicts of interest and suggests ways of dealing with them. Part IV highlights the significance of preserving confidentiality by SSB members and recommends that IIFS have a risk management strategy in place in the event of damaging leakage. Part V is concerned with enhancing the consistency of SSB decisions, which is vital to strengthening SSBs’ credibility and integrity. It suggests best practises when consensus decision cannot be reached by SSB members.¹¹⁷² In short, the standard provides solutions for the SSB governance issues discussed extensively in chapter five.

IFSB acknowledges that with regard to a Shari‘ah governance framework, there is no “single model” or “one-size-fits-all” approach. An IIFS should adopt a Shari‘ah governance structure that is appropriate and adequate for its size, the nature of its business and its complexity. Different jurisdictions might take different approaches to this matter. While some national regulators follow a more centralised approach for Shari‘ah governance, others have decided to leave it to the market to decide what system of governance is sufficient to provide the credibility for its Shari‘ah-compliant

¹¹⁷¹ "IFSB Guiding principles on Shariah governance systems for institutions offering Islamic financial services" p8.

¹¹⁷² *ibid.*, p5.

products and services. IFSB stresses that stakeholders should share the responsibility for ensuring a sound and effective Shari‘ah governance structure. This task should not only be the burden of SSB members. Rather, regulatory bodies, management, and consumers should play a role in ensuring the effectiveness of the Shari‘ah governance structure.¹¹⁷³

Other standards of IFSB include many principles which can also be relevant to the issue of Shari‘ah compliance. For example, the first principle of the IFSB Guiding Principles on Conduct of Business (IFSB-9) is about honesty and fairness. It states that an IIFS should be careful not to intentionally or accidentally mislead stakeholders about the Shari‘ah compliance of its products or services, or to mislead consumers by withholding substantial information.¹¹⁷⁴ Noncompliance with this principle is further illustrated by the example of manipulating the process for obtaining SSB approval by not disclosing substantial information that the Shari‘ah board needs to ensure the Shari‘ah compliance of a particular product.¹¹⁷⁵ In addition, where the Shari‘ah compliance of a product (e.g., some *sukūk* structures) is disputed among Shari‘ah scholars, the principle of due care and diligence can be exercised by taking into account that some investors from different geographical areas might follow a school of thought that deems the structure of such a product as non-Shari‘ah compliant. As a result, these investors might find themselves forced to dispose of this product, possibly at a loss, and to donate any profit to charity.¹¹⁷⁶ Furthermore, principle seven of the IFSB Guiding Principles on Conduct of Business states that an IIFS must be able to show that its business activities are governed by an efficient system of

¹¹⁷³ Ibid., p4.

¹¹⁷⁴ "Guiding Principles on Conduct of Business for Institutions offering Islamic Financial Services (IFSP-9) " IFSB,, http://www.ifsb.org/standard/IFSB-9_Guiding%20Principles%20on%20Conduct%20of%20Business.pdf. accessed 28 May 2013

¹¹⁷⁵ Ibid., p5.

¹¹⁷⁶ Ibid., p7.

Shari‘ah governance and that it manages its operations in a socially responsible way.¹¹⁷⁷

However, despite the participation of many national regulators on IFSB committees, its guidelines and standards are not binding.¹¹⁷⁸ Malaysia, the host country of the IFSB, might be the only notable example which incorporated a lot of the IFSB standards into its national legal framework. On the other hand, Saudi Arabia, an active IFSB member, has not adopted any IFSB standards related to Islamic finance and Shari‘ah governance.¹¹⁷⁹ There is a lack of literature regarding the actual impact of IFSB standards on the practises of the Islamic finance industry. In fact, a study conducted by Zulkifli Hasan suggests that IIFS have a low level of awareness about the development of Shari‘ah governance standards and best practises.¹¹⁸⁰ More than 22% of the surveyed Islamic financial institutions had no knowledge about existence of the IFSB Guiding Principles on Shari‘ah Governance Systems (IFSB-10), and only 45.7% of Islamic financial institutions have implemented the AAOIFI governance standards. Nevertheless, the IFSB effort provides a strong infrastructure for developing the Islamic finance industry and for harmonising Islamic finance national regulations across the globe.

Indeed, there are other international organisations which generally contribute to the development of Islamic finance. One example is the General Council for Islamic Banks and Institutions (CIBAFI),¹¹⁸¹ which aims to promote research and development in Islamic finance as well as product registration. Another example is

¹¹⁷⁷ Ibid., p15.

¹¹⁷⁸ Bahrain's central banker supports making IFSB standards mandatory: Blake Goud, "Bahrain's Central Banker Supports Making IFSB Standards Mandatory," Sharing Risk, <http://investhalal.blogspot.co.uk/2013/01/bahrains-central-banker-supports-making.html>. accessed 25 May 2013

¹¹⁷⁹ See: Saudi Regulators' Approach towards Shari‘ah Governance p228.

¹¹⁸⁰ Hasan, "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK," p320.

¹¹⁸¹ The General Council for Islamic Banks And Financial Institution (CIBAFI), "About CIBAFI," CIBAFI, <http://www.cibafi.org/Pages.aspx?id=pvRm8sofDxI=>. accessed 16 May 2013

the International Organization of Securities Commissions (IOSCO), which has issued a special report analysing the application of its own objectives and principles of securities regulation for Islamic securities products.¹¹⁸² It recommends national regulators define their approach towards regulating Shari‘ah compliance,¹¹⁸³ and it suggests that regulators who are involved in determining Shari‘ah compliance disclose key resolutions and the reasoning behind them. Moreover, it encourages regulators to ask IIFS to adopt a Shari‘ah-compliant risk management strategy.¹¹⁸⁴

The four external mechanisms discussed thus far—Shari‘ah compliance ratings, Shari‘ah indices, private Shari‘ah auditing, and the adoption of international standards related to enhancing Shari‘ah compliance—can be buttressed by the judicious application of the following internal mechanisms to remedy creative Shari‘ah-compliance.

7.6. Whistle Blowing

One of the remedies which can be used to remedy creative Shari‘ah-compliance in the Islamic finance industry is to legally authorise SSB members to blow the whistle if their decision has been ignored or if they see a serious breach of Shari‘ah compliance with the management and board of directors refusing to take action.¹¹⁸⁵ In addition, whistle blowing is important to secure compliance, since direct access to shareholders might not always be available to SSBs; even if they do have access, dominant shareholders might not be interested in a dispute between the SSB and the management, with whom they likely have a close relationship.¹¹⁸⁶ Rider¹¹⁸⁷ questions

¹¹⁸² Executive Committee of IOSCO, "Analysis of The Application of IOSCO's Objectives And Principles of Securities Regulation For Islamic Securities Products " International Organization of Securities Commissions (IOSCO), <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD280.pdf>. accessed 17 June 2012

¹¹⁸³ Ibid.

¹¹⁸⁴ Ibid., p34.

¹¹⁸⁵ See: Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," p170.

¹¹⁸⁶ Ibid.

whether SSB members can realistically be expected to blow the whistle, given that they are usually appointed and compensated by IIFS management or the board of directors. Would it be morally right for SSB members not to do more than raise the matter with management? Do scholars, in the eyes of Shari‘ah, have a responsibility to take further actions such as reporting the matter to regulators or issuing a public statement? Muslims in general and particularly those who have Shari‘ah knowledge are prohibited from concealing the truth.¹¹⁸⁸ Verse 2:259¹¹⁸⁹ of the Quran reads, “Indeed, those who conceal what We sent down of clear proofs and guidance after We made it clear for the people in the Scripture—those are cursed by Allah and cursed by those who curse”. Additionally, verse 3:187 reads, “And [mention, O Muhammad], when Allah took a covenant from those who were given the Scripture, [saying], ‘You must make it clear to the people and not conceal it’. But they threw it away behind their backs and exchanged it for a small price. And wretched is that which they purchased”.¹¹⁹⁰ Another *ḥadīth* of the prophet Muhammad states, “He who is asked about knowledge [of religion] and conceals it, will be bridled with a bridle of fire on the Day of Resurrection”.¹¹⁹¹

However, SSB members might not be able to blow the whistle in non-Islamic jurisdictions even if they wanted to do so, since regulators in countries where a special framework of Islamic finance is absent might not be officially interested to hear about non Shari‘ah-compliant incidents, as long as an IIFS is in compliance with the conventional legal framework. In fact, blowing the whistle in this case might hold

¹¹⁸⁷ Ibid.

¹¹⁸⁸ Mohammad al-Othaimeen, "al-Taḥdhīr min al-Fatawā bighar ‘ilm, al-Taḥdhīr min Kutmān al-‘ilm," *Ibnothaimeen.com*, http://www.ibnothaimeen.com/all/khotab/article_121.shtml. accessed 23 July 2013.

¹¹⁸⁹ Saheeh International, *Translation Of The Meanings Of The Glorious Quran*.

¹¹⁹⁰ Ibid.

¹¹⁹¹ Abu Dawud, "Sunan Abi Dawud: Knowledge (Kitab Al-Ilm)," *Sunnah.com*, <http://sunnah.com/abudawud/26/18>. accessed 19 May 2013

SSB liable for breaching the confidentiality provision in their contract and their fiduciary duty, as well as for interfering with the business of IIFS.¹¹⁹² Moreover, they might be sued by the IIFS in question for defamation.

Nevertheless, regulators ought to avoid uncertainty in this situation and arrange a channel of communications with SSBs so that members can report their concerns. Doing so is crucial because if a serious breach of Shari'ah compliance comes to light, it might cause consumers to lose confidence in the IIFS and boycott its products and services. This would affect the IIFS credit profile and ultimately have an impact on the stability of the financial system. In Malaysia, SSB members will not be in breach of the confidentiality and secrecy code if they report serious non-Shari'ah compliance to Bank Negara Malaysia in good faith.¹¹⁹³

In fact, the Islamic Financial Services Board suggests in its Guiding Principles on Conduct of Business for Institutions Offering Islamic Financial Services (IFSP-9)¹¹⁹⁴ that all IIFS should have a whistle-blowing policy in place. It should embolden IIFS personnel to immediately notify the management about any suspected violation of business conduct principles. The policy should explain the procedures for reporting such incidents, the actions that the management must take when it learns about the violation, and the IIFS's duties to prevent the violation from reoccurring.

7.7. Characterising the Articles of Association

A second internal mechanism for strengthening Shari'ah compliance in Islamic financial institutions is for IIFS to characterising themselves in their articles of

¹¹⁹² Rider, "Corporate Governance of Institutions Offering Islamic Financial Services," p170.

¹¹⁹³ Bank Negara Malaysia (BNM), "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)" p20.

¹¹⁹⁴ Islamic Financial Services Board (IFSB), "Guiding Principles on Conduct of Business for Institutions offering Islamic Financial Services (IFSP-9) " p4.

association as an entity that fully complies with Shari‘ah ruling.¹¹⁹⁵ This remedy can be used in particular where an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari‘ah governance. IIFS articles of association can include provisions for setting up an SSB and defining its power;¹¹⁹⁶ the duties of its members; the policy of appointing, dismissing, and fixing remuneration of SSB members; and the process of ensuring Shari‘ah compliance. Moreover, IIFS articles of association should include a default clause which identifies the relationship between the board of directors and the SSB and the applicable procedure in case a conflict arises between the two boards.

In Saudi Arabia, for example, where there is no framework for Shari‘ah governance in the financial sector,¹¹⁹⁷ Al Rajhi Bank has clarified its policy towards the power of its SSB. It regards SSB decisions as obligatory for the departments and management of the institution, and it makes executive directors at all levels responsible for implementing SSB resolutions. Any violation of SSB pronouncement while offering products or services, without prior authorisation from the board, is firmly outlawed, and all violators are disciplined.¹¹⁹⁸ Such steps seem to be more visible than the involvement of regulators, especially in non-Muslims countries.

7.8. Conclusion

This chapter has suggested six private mechanisms to remedy creative Shari‘ah compliance and addressed their limitations. These mechanisms include adopting a Shari‘ah compliance rating, Shari‘ah indices, private Shari‘ah auditing, international standards related to enhancing Shari‘ah compliance, and a whistle-blowing policy for

¹¹⁹⁵ Mahmood, "Islamic Governance, Capital Structure, and Equity Finance: Examining the Possibilities of American Financial Shari'ah Boards."

¹¹⁹⁶ Garas and Pierce, "Shari'a Supervision of Islamic Financial Institutions," p389.

¹¹⁹⁷ Hasan, "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK," p97.

¹¹⁹⁸ Alrajhi Bank, "The Sharia Group".

serious Shari'ah-compliance violations, as well as characterising an IIFS in its articles of association as an entity that fully complies with Shari'ah ruling.

The implementations of these measures involve major players in the industry, such as central banks, SSBs, private Shari'ah auditing firms, rating agencies, international standard-setting bodies, and shareholders. These remedies can be used in particular where an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari'ah governance.

Conclusion

This thesis has investigated the issue of creative Shari‘ah compliance in the Islamic finance industry with a focus on the regulatory approach in Saudi Arabia and the UK. Creative Shari‘ah compliance can be defined as compliance with the letter but not the objectives of Shari‘ah. As the introduction to this study showed, Islamic finance industry practises have come under scrutiny in recent years, with strong critiques levelled against many institutions that claim to provide Shari‘ah-compliant Islamic financial products and services, while such services or products in fact undermine the spirit and the objectives of Shari‘ah. Financial instruments based on the profit- and loss-sharing model are deemed by Shari‘ah scholars and Muslim economists to be the most compliant with the objectives of Islamic law. Nonetheless, research has shown that they are the least practised forms of Islamic finance; in contrast, institutions offering Islamic financial services (IIFS) offer mainly debt-based instruments.

While many researchers have noted this gap between the theory and practise of Islamic finance, no study has provided a sustained analysis of the issue. This thesis undertakes such analysis and, in doing so, significantly contributes to the sphere of Islamic finance in three main ways. First, it critically appraises justifications of creative Shari‘ah compliance practises. Second, it examines how Shari‘ah supervisory board (SSB) governance practises and the inconsistent *fatwas* issued by SSBs contribute to the issue of creative Shari‘ah compliance in contemporary Islamic finance. Most importantly, it suggests regulatory mechanisms which regulators can employ in Islamic countries such as Saudi Arabia and in secular countries such as the United Kingdom to deal with the issue of creative Shari‘ah compliance.

Chapter one of this thesis provided an overview of Islamic law and its key features. The main sources of Shari‘ah are the Quran and the *sunnah*. The secondary sources include *ijma* (consensus), *qiyas* (analogical reasoning), and *urf* (custom). Many different *sunnī* schools of thought have been formed, including the main four *sunnī* schools which remain in the Islamic world today, namely the Ḥanafī School, the Mālikī School, the Shāfi‘ī School, and the Ḥanbalī School. In Shari‘ah, the starting assumption of all contracts is their permissibility. However, for a contract to be Shari‘ah-compliant, it must avoid certain prohibitions. These include *ribā* (usury), *gharar* (excessive risk or uncertainty), and *maisir* and *qim‘ar* (gambling). The chapter categorised Shari‘ah-compliant financial instruments into two broad groups, equity-type contracts and debt-financing contracts, and detailed some examples of instruments in each group.

In addition, chapter one gave an overview of the objectives of Islamic law. Muslim legal theorists agree that the overall objective of Shari‘ah is to bring benefit to and remove harm from all human beings. In particular, Shari‘ah promotes well-being by protecting five essential principles: the preservation of religion (*dīn*), the preservation of life (*nafs*), the preservation of intellect (*‘aql*), the preservation of posterity (*nasl*), and the preservation of wealth (*māl*). Anything that contributes to the preservation of these five principles benefits the public and is desired, while anything that harms them is against the public interest and its elimination is required. The principles of Islamic finance seek to realise social justice through the circulation of resources, efficiency in consumption, and satisfying people’s basic needs. The prohibition of *ribā* and *gharar* serves to achieve the same result of social justice. *Ribā* is seen as an unjustified growth in wealth at the cost of the fair circulation of resources, while the uncertainty caused by *gharar* potentially leads to disputes within

the community. The prohibition of *riba* suggests that cooperative and participatory funding (equity-based financing) is the ideal form of financing in Shari‘ah; it is regarded as a mechanism for the fair mobilisation of wealth, which increases productivity and achieves the well-being of the people.

Chapter two examined whether creative Shari‘ah compliance is a phenomenon new to Islamic law. Classical Shari‘ah scholars have addressed the practise of creative Shari‘ah compliance under the term *hīlah*. The chapter investigated the position of Islamic schools of thought on *hīlah* and its interrelationship with the debate on form and substance in Islamic finance. It surveyed whether classical Islamic jurisprudence provides a justification for using *hīlah* (a legal ruse) to practise creative Shari‘ah compliance.

This chapter’s key argument is that addressing the issue of form and substance in Islamic finance necessitates a distinction between two connotations: permissibility (*ṣaḥīḥ diyānatan*) and validity (*ṣaḥīḥ qaḍā’an*). In Islam, every action generally has two dimensions: hidden and manifest. “Permissibility” here refers to the inward, hidden dimension of a contract, where it is characterised, for example, as prohibited or permissible. It concerns the accountability of a person to Allah in the hereafter. “Validity” refers to the outwardly manifest dimension of a contract, where a judge rules whether it is valid and thus legally enforceable or not. The outward dimension concerns individuals’ rights in this world.

From a permissibility perspective, the research concluded that there is no authority for utilising a form to circumvent the spirit of Shari‘ah law in finance. However, from a judicial validity perspective, if such a form had been used in a contract and disputed before a judge, it could be deemed valid according to some schools of thought, including Ḥanafī and Shāfi‘ī. In addition, some classical jurists accepted some *hīlah*

on individual cases as exceptions to the general rule or to the judicial context. However, applying *hīlah* on a systemic level, as many financial institutions currently do, removes its legitimacy. Accordingly, Shari‘ah supervisory boards should not rely on such precedents to structure or Islamise financial products. Modern economic and finance knowledge put contemporary scholars in a better position than classical jurists were to determine whether a certain product complies with the spirit of Islamic law or not. Insisting on justifying the use of some *hīlah* because it was mentioned in the classical literature would only harm the industry of Islamic finance. Ultimately, people would come to realise that there is no difference between conventional products and so-called Shari‘ah-compliant products except that the latter are more expensive.

Chapter three illustrated creative Shari‘ah compliance in the Islamic finance industry by examining *tawarruq*, one of the most common structures used by IIFS. After defining *tawarruq* and its various forms, the chapter addressed Shari‘ah scholars’ views on the permissibility of *tawarruq*. It showed that while most scholars deem jurisprudential *tawarruq* as *makrūh* (discouraged, but not prohibited), the majority of scholars deem the organised *tawarruq* used by IIFS prohibited; they see it as *hīlah* (a legal ruse) to circumvent the Shari‘ah prohibition on *ribā* (usury). The ultimate goal of organised *tawarruq* structures is to provide a sum to be paid later with a fixed return. IIFS and their clients are not interested in the underlying commodity, which is only used as a means to overcome the Shari‘ah restriction against giving a usurious loan. Last, the chapter argued that organised *tawarruq* is worse than *ribā* since it casts doubt on the authenticity of Shariah-compliant products; does not carry any social, economic, or equity benefits; and has the same disadvantages as a usurious loan.

Chapter four examined the inconsistency in the *fatwas* issued by Shari‘ah supervisory boards that reside in IIFS as a key factor contributing to the issue of creative Shari‘ah compliance. It addressed the debate for and against standardisation. It investigated the causes of juristic differences, namely, variable Quranic recitation, using words with multiple meanings, lack of knowledge of *ḥadīth*, adopting certain legal principles, disregarding the change of *maṣlahah* (public interest), and the structure of the *fatwa*. The chapter concluded that juristic differences are inevitable because Islamic law has not been received as ready-made rules for implementation. Unlike modern laws, where interpretation is not always required, in Shari‘ah, interpretation of its sources is necessary to understand the intention of the lawgiver. The interpretation process does not take a speculative nature, but is rather governed by a well-stated approach and methodical tool known as *ijtihād*, which a jurist uses to extract the law on a given matter.

The chapter argued that juristic differences pose a serious challenge to compliance in the Islamic finance industry. It assessed the aptness of standardisation as a remedy for inconsistencies in *fatwas* issued by SSBs. It further argued that it is possible for a state to enforce a particular Shari‘ah interpretation, and that such a solution has been justified by classical and contemporary Shari‘ah jurists. However, it might be difficult to use this remedy at a global level due to the lack of political will or legal power to regulate religious matters in secular countries. Accordingly, this chapter suggested that efforts be directed towards establishing a Shari‘ah standard which codifies various practises of Islamic finance, even if they are deemed highly controversial. Such well-defined standards would facilitate the task of regulators, courts, and rating agencies, as well as gradually encouraging IIFS to be more transparent with their clients about which *fatwa* or school of thought they are adopting, rather than using the

general label of “Shari‘ah compliant”. With such a level of disclosure, the market would hopefully move towards adopting best practises.

Chapter five explored definitions of SSBs in the Islamic finance literature as well as highlighting their importance in IIFS structure. For IIFS to gain the trust of their Muslim clients, they normally incorporate a religious board in the form of an SSB. In theory, the function of the SSB is to ensure that IIFS operate within Shari‘ah norms and teachings. The chapter examined the impact of regulatory issues surrounding SSBs on Shari‘ah compliance in the contemporary Islamic finance industry, identifying seven challenges as major factors contributing to the issue of creative Shari‘ah compliance in IIFS. These are SSBs’ unclear functions and legal status, lack of accountability and transparency, and conflicts of interest and lack of independence, as well as the poor training and inadequate qualifications of SSB members.

The chapter put forth a few suggestions to confront these challenges. Crucially, it stressed that to maintain sound financial systems and investor confidence, regulators in Islamic and secular countries have to recognise the need for their involvement in regulating Shari‘ah governance in IIFS. In other words, a solid Islamic financial market cannot be established unless Shari‘ah governance is regulated, ideally by a centralised body. In addition, Shari‘ah supervision should be recognised as an independent profession. Like lawyers and accountants, its members should act within a framework that defines their legal status, role, and responsibilities. In cases where an IIFS is operating within a jurisdiction which does not favour Islamic finance or where regulators are passive, SSB members can take a proactive role in regulating Shari‘ah governance by working across SSBs to standardise their own contracts with financial institutions. Emphasising accountability and transparency in SSBs should not be perceived as showing less respect to Shari‘ah scholars or doubting their

credibility, but rather as dealing professionally with an essential group in the industry and adding a layer of protection to public interests. This is particularly important if IIFS are operating in a global market where the local reputation of Shari‘ah board members may not be sufficient to allay stockholders’ suspicions over their reliability or SSBs’ lack of accountability and transparency.

Chapter six suggested two public mechanisms where a national body is involved in remedying the issue of creative Shari‘ah compliance. The first one is to establish a central Shari‘ah supervisory board (CSSB), either as a self-regulatory body or as a unit within the central bank which would oversee the Shari‘ah governance and the implementation of Islamic finance in the financial industry. The chapter examined the central Shari‘ah boards in Sudan and Malaysia to offer a better understanding about the nature of CSSBs’ work. The chapter then discussed the attitudes of regulators in the UK and KSA towards Shari‘ah governance and CSSB in detail.

This remedy might not be desirable in some countries mostly because establishing a central Shari‘ah board is deemed a religious matter that is beyond the legal authority of a secular regulator. Nevertheless, this chapter argued that making sure that IIFS have an adequate process of ensuring Shari‘ah compliance and that SSBs have a proper corporate governance culture does not conflict with the secular nature of a regulator. Moreover, this chapter argued that regulators risk breaching their obligation to protect consumers, one of the main objectives of setting up a financial service authority, if they do not regulate Shari‘ah governance and do not try to prevent creative Shari‘ah compliance in IIFS. The current approach followed by the FCA in the UK and SAMA in KSA with regard to Shari‘ah governance is not adequate to protect consumers from creative Shari‘ah compliance. The FCA and SAMA ought to

strongly encourage IIFS and other relevant organisations in the UK and Saudi to at least form a self-regulatory body for the Islamic finance industry.

The second public mechanism this chapter proposed was increasing the level of disclosure which regulators require from IIFS. This tool can particularly be utilised by regulators in secular countries to increase consumer protection without the need to enact a Shari'ah governance framework. Consumers should be fully aware about the role and the status of SSBs to be able to make an informed decision. They should be able to trust that an IIFS is truly Shari'ah compliant if it presents itself that way. In particular, regulators should enhance disclosure in two areas: the Shari'ah governance of IIFS and the annual report of SSB. The chapter suggested that Shari'ah auditing should follow the practise of conventional auditing, where four types of auditing opinions are recognised, namely, unqualified opinion, qualified opinion, adverse opinion, and disclaimer. In addition, regulators need to set further requirements for disclosures in relation to non-Shari'ah income purification. For example, what is the value of the income, how much was purified during the period of the financial statement, and why was the remainder not purified? It also should indicate the nature of the charities which benefit from the purification process and their relationship to the IIFS, and include a statement confirming that the IIFS has not benefited from the money allocated for purification. Finally, the chapter recommended adopting the IFSB Standard on Transparency and Market Discipline (IFSB-4), which would provide a high level of disclosure and would increase the transparency within the industry, helping consumers to make an informed decision.

Chapter seven proposed six private mechanisms to remedy creative Shari'ah compliance which can be employed without governmental involvement. The first one is a Shari'ah compliance rating, where an IIFS or a product is rated according to its

compliance with the objectives of Islamic law. The chapter discussed the experience of the Islamic International Rating Agency (IIRA), one of the first rating agencies to issue a rating based on Shari'ah compliance. It argued that the Shari'ah compliance rating as described in the IIRA methodology is unlikely to improve the level of Shari'ah compliance in the industry. This is because IIRA only conducts Shari'ah ratings at the request of an IIFS, and the result will not be published without the permission of the IIFS. This means that only good ratings will be published, as no IIFS would agree to publish a negative rating. IIRA seeks the approval of an IIFS before rating its Shari'ah compliance, because IIRA does not want to have any negative impact on the industry. This may suggest that IIRA aims to promote IIFS business rather than increasing the compliance level and protecting consumers. IIRA and other rating agencies should conduct unsolicited Shari'ah compliance ratings based on the information disclosed by IIFS, as is the case in credit ratings. This would encourage IIFS to disclose more information about their Shari'ah-compliant products and Shari'ah governance structure. Shari'ah compliance ratings should be carried out by more independent rating agencies, and a higher weight should be given to the substance of products in the results of the rating. This would generally increase the level of Shari'ah compliance in the industry.

The second suggested private mechanism is the use of Shari'ah indices. These indices were initially developed for Shari'ah-compliant investment in stock markets. An index can be issued individually by Shari'ah scholars or in a more organised way by financial institutions such as credit rating agencies. The chapter examined one of the first attempts to create a Shari'ah-compliant index, the Dow Jones Islamic Market Index (DJIMI), and addressed its shortcoming. The calculation method for these indices is generally based on the business activities and the debt structure of the listed

companies. This method of composing Shari‘ah-compliant indices is fairly controversial among Shari‘ah scholars. Besides that sentiment, there is the question of whether financial statements represent a reliable way to screen for non-Shari‘ah-compliant liability and assets. In short, neither Islamic indices nor Shari‘ah quality ratings as currently practised by IIRA represent the desired form of Shari‘ah compliance rating.

The third proposed private mechanism is the use of private Shari‘ah auditing firms (SAFs). This thesis argued that the task of designing and approving Shari‘ah-compliant products should be separated from the task of ensuring their compliance. While the internal SSB can approve Shari‘ah-compliant products (*ex ante* review), SAFs should conduct the *ex post* review to mitigate the risk of self-review. SAFs would verify that the implementations of these structures approved by the internal SSB are in line with objectives of Shari‘ah. The chapter highlighted some of the limitations of this mechanism. For one, the lack of a legal framework for SAF activities resulted in unprofessional governance practises, including potential cases of conflict of interest, breach of confidentiality, and inappropriate competition between SAFs. Moreover, an SAF decision is not binding on IIFS. Therefore, Shari‘ah compliance might be questioned if an SAF is acting as the SSB of the bank. IIFS might not want to restrict themselves to one SSB, since using SAFs’ *fatwa* services can offer more flexibility for product approval. This may explain why SAFs are widely used by conventional institutions offering Islamic windows. This brings up the issue of “*fatwa* shopping”, where IIFS search the market seeking approval for a particular product. In this sense, SAFs contribute negatively to Shari‘ah compliance and actually facilitates the practise of creative Shari‘ah compliance. To solve these issues, the chapter recommends that regulators consider a legal framework; establish a

supervisory body, preferably a self-regulated one, to license and oversee SAF conduct; ensure compulsory reporting; and preserve confidentiality and transparency. This framework should help to define the scope and procedures of SAF services, and how their work is different from that of SSBs, internal Shari‘ah auditors, and external financial auditors.

The fourth proposed private mechanism is adopting international standards related to enhancing Shari‘ah compliance. In particular, the chapter discussed two international standard-setting bodies which have been actively engaged with the Islamic finance industry. Those are the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB). The former’s standards are more directed towards individual IIFS, while the latter’s standards are more focused on national regulators. IFSB has so far issued four standards relevant to the discussion of this research. These are the standards on Guiding Principles on Shari‘ah Governance System (IFSB-10), Conduct of Business for Institutions Offering Islamic Financial Services (IFSB-9), Corporate Governance (IFSB-3), and Transparency and Market Discipline (IFSB-4).

This chapter highlighted two limitations to the effectiveness of international standards as a mechanism to remedy creative Shari‘ah compliance. First, concerns have been raised about the regulatory independence of AAOIFI. There is no assurance that standards and frameworks introduced by this entity follow public interests and are not affected by regulatory capture. Second, despite the participation of many national regulators on IFSB committees, its guidelines and standards are not binding. Malaysia, the host country of the IFSB, might be the only notable example which incorporated many of the IFSB standards into its national legal framework. On the

other hand, Saudi Arabia, an active member in IFSB, has not adopted any of the IFSB standards related to Islamic finance and Shari'ah governance.

The fifth proposed private mechanism is to legally authorise SSB members to blow the whistle if their decision has been ignored or if they see a serious breach of Shari'ah compliance with management and the board of directors refusing to take action. This chapter argued that whistle blowing is important to secure compliance, since direct access to shareholders might not always be available to SSBs. Even if they do have access, dominant shareholders might not be interested in a dispute between the SSB and the management, with whom they likely have a close relationship. However, this mechanism has some limitations. SSB members might not be able to blow the whistle in non-Islamic jurisdictions even if they wanted to do so. This is because regulators in countries where a special framework of Islamic finance is absent might not be officially interested to hear about non Shari'ah-compliance incidents, provided that the IIFS is in compliance with the conventional legal framework. In fact, blowing the whistle in this case might leave SSB members liable for breaching the confidentiality provision in their contract and their fiduciary duty, as well as interfering with the business of their IIFS. Moreover, they might be sued by the IIFS in question for defamation. Nevertheless, regulators ought to avoid uncertainty in this situation and arrange a channel of communications with SSBs for members to report their concerns. If a serious breach of Shari'ah-compliant comes to light, it might cause consumers losing confidence in the IIFS and boycotting its products and services. This would affect the IIFS credit profile and ultimately have an impact on the stability of the financial system.

The last proposed private mechanism is characterising an IIFS in its articles of association as an entity that fully complies with Shari'ah ruling. The articles of

association of an IIFS can include provisions for setting up an SSB and defining its power; the duties of its members; its policy of appointing, dismissing, and fixing remuneration of its members; and its process of ensuring Shari‘ah compliance. Moreover, IIFS articles of association should include a default clause identifying the relationship between the board of directors and the SSB and the applicable procedure in case a conflict arises between the two boards. Such a step seems to be more visible than the involvement of regulators, mainly in non-Muslims countries. These mechanisms discussed in chapter seven can be used in particular where an IIFS is operating within a jurisdiction where regulators cannot or prefer not to be involved in regulating Shari‘ah governance. The implementations of these measures involve major players in the industry, such as SSBs, private Shari‘ah auditing firms, rating agencies, international standard-setting bodies, and shareholders.

This research has raised many questions in need of further investigation. The first one is whether the current financial system, and particularly the banking sector, will ever be an appropriate venue for offering authentically Shari‘ah-compliant products. Commercial banks play the role of a financial intermediary by accepting deposits and lending money at interest. The profit- and loss-sharing model which is the ideal form of financing in Islam is alien to the banking environment. Accordingly, further attempts to “Islamise” the practise of banks might lead to promoting creatively Shari‘ah-compliant products, such as *tawarruq*, which try to replicate the outcome of debt-based conventional products. Another question worth investigating is the role of lawyers in contributing to the issue of creative Shari‘ah compliance. Although Shari‘ah products are ultimately approved by the SSB, lawyers are heavily involved in structuring Shari‘ah-compliant products. Many top law firms have teams of lawyers dedicated to the needs of the Islamic finance industry. Finally, the discussion of this

thesis has been theoretical, with examples mainly from retail banking. There is thus a need to conduct empirical studies about the existence and the size of creative Shari‘ah compliance practises in other areas of the financial industry, including the insurance market and the capital market.

Bibliography

Bibliography

- ABC International Bank plc (ABCIB). "Shariah Compliance." ABCIB,,
http://www.alburaq.co.uk/shariah_compliance.asp. accessed 28 August 2011
- Abd Hamid, Mohd Shahrulnizam. "Shariah Interpretation Inconsistencies in Takaful Operation." *INCEIF*, .
http://www.academia.edu/399303/Inconsistencies_in_Shariah_Interpretations_The_Takaful_Experience accessed 10 July 2012
- Abd Jabbar, Siti Faridah. "Financial crimes: Prohibition in Islam and prevention by the Shar'a Supervisory Board of Islamic financial institutions." *Journal of Financial Crime* 17, no. 3 (2010): 287-94.
- Abd Jabbar, Siti Faridah "The Governance of Shari'a Advisers of Islamic Financial Institutions: The Practice in Malaysia." *The Company Lawyer* 30, no. 10 (2009): 312-14.
- Abd Jabbar, Siti Faridah "International - The Shari'a Supervisory Board: a Potential Problem in Islamic Finance." *The Company lawyer* 29, no. 1 (2008): 29.
- Abd Jabbar, Siti Faridah "Sharia-Compliant Financial Instruments: Principles and Practice." *The Company Lawyer*. 30, no. 6 (2009): 176.
- Abd Jabbar, Siti Faridah "The Sharia Supervisory Board of Islamic Financial Institutions: A Case for Governance." *The Company Lawyer* 30, no. 8 (2009): 243-48.
- ‘Abdālbar, Muḥamaad Zakī. *Taqnīn al-Fiqh al-Islāmī*. edited by ‘AbdAllāh al-Anṣārī: Dār al-Turāth al-Islāmy, 1986.
- Abdul-Rahman, Yahia. *The Art of Islamic Banking and Finance : Tools and Techniques for Community-Based Banking*. Hoboken, N.J.: Wiley, 2010.
- Abdul Alim, Emmy "Malaysia Seeks to be Global Educational Hub." *The Islamic Globe*,
http://www.theislamicglobe.com/index.php?option=com_content&view=article&id=282:malaysia-seeks-to-be-global-educational-hub&catid=17:survey&Itemid=74.
accessed 23 May 2011
- Abdulaziz AlGasim Law Firm. "al-Khadamāt al-Māliyyah al-Islāmiyyah fī al-Mimlakh al-‘arabiyaah al-Su‘ūdiyyah: al-Tanmiyyah wa al-Ḥawkamah." Riyadh, 2009.
- Abozaid, Abdulazeem, and Asyraf Wajdi Dusuki. "The Challenges of Realizing Maqasid al-Shari`ah in Islamic Banking and Finance." Paper presented at the IIUM International Conference on Islamic Banking and Finance: ‘Research and Development: The Bridge between Ideals and Realities’, Kuala Lumpur, 23rd – 25th April 2007.
- Abū Ghuddah, ‘Abd al-sattār "al-Usus al-Fanniyyah lil-rraqābah al-Shar‘iyyah Wa ‘Alāqatuhā Biālttadqīq al-Shar‘ī Fī al-Mu‘asasāt al-Māliyyah al-Islāmiyyah ".
ḥawliyyah al-Barakah 4, no. November (2002): 8.
- Abū Yūsuf, Ya‘qūb Ibrāhīm. *Kitāb al-Kharāj*. Dār al-Ma‘rifh, 1979.
- Abū Zahrah, Muḥammad. *Abū Ḥanīfah Ḥaātuh wa ‘Aṣruḥ Arā‘uh wa Fiqhuh*. Dār al-Fikr al-‘Arabī, 1991.
- Abumouamer, Faris Mahmoud. "An Analysis of the Role and Function of the Shariah Control in Islamic Banks." PhD thesis, University of Wales, College of Cardiff, 1989.
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). " No. 1 - Shari’a Supervisory Board: Appointment, Composition and Report." In *AAOIFI Governance Standard for Islamic Financial Institutions*. Bahrain: AAOIFI, 1999
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). "AAOIFI Key Publications." AAOIFI,

- <http://www.aoifi.com/aoifi/Publications/KeyPublications/tabid/88/language/en-US/Default.aspx>. accessed 23 May 2013
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). "Accounting, Auditing & Governance Standards for Islamic Financial Institutions " In *Shari'a Review*. Bahrain: AAOIFI, 2002.
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). "Certified Islamic Professional Accountants (CIPA)." AAOIFI, <http://www.aoifi.com/aoifi/ProfessionalDevelopment/CertifiedIslamicProfessionalAccountantCIPA/tabid/76/language/en-US/Default.aspx>. accessed 14 May 2013
- Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). "Overview." AAOIFI, <http://www.aoifi.com/aoifi/TheOrganization/Overview/tabid/62/language/en-US/Default.aspx>. accessed 18 May 2013
- Ahli United Bank (UK) (AUB). "Annual Report." http://www.ahliunited.com/pdfs/ar/AUB_AnnualReport_2010.pdf. accessed 28 August 2011
- Ahli United Bank (UK) (AUB). "Our Sharia'h Board " www.iibu.com/shariaa_board/sboard.aspx. accessed 28 August 2011
- Ahmad, Abu Umar Faruq, and Muhammad Fazlul Karim. "Legal and Regulatory Issues in Islamic Finance Industry: The Evidence from UK and Australia." *6th International Islamic Finance Conference* (2008). <http://www.kantakji.com/fiqh/Files/Markets/c35.pdf> accessed 10 November 2010
- Ahmad, Ahmad Muḥī al-dīn "Hudūd al-Hay'āt al-Shar'īyyah Wa Idārāt al-Mu'assasāt al-Māliyyah al-Islāmiyyah Fī al-Ta'akud min al-Āltizām Biāl' Ahkām al-Shar'īyyah " Paper presented at the Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 5-6/10/2003.
- Ahmad, Muḥammad 'Alī Yūsuf "Dawr al-Suluṭāt al-Riqābiyyah Fī al-Riqābah 'Alā al-Mu'assasāt al-Māliyyah al-Islāmiyyah " Paper presented at the The 2nd Conference of Islamic Financial Services., Tripoli-Libya, 27-28/4/2010.
- Aḥmad , Muḥy al-Dīn Aḥmd " al-Taṭbīqāt al-Maṣrifīyyh li'aqd al-Tawarruq." Paper presented at the Dawr al-Mu'sasāt al-Maṣrifīyyah fī al-āstithmār wa al-Tanmiyyah, Sharjah, UEA, 7-9 May 2002.
- Ahmed, Habib. "Defining Ethics in Islamic Finance: Looking Beyond Legality " Paper presented at the 8th International Conference on Islamic Economics and Finance, Doha, 18th December 2011.
- Ahmed, Habib. "Islamic Finance at a Crossroads: the dominance of the asset-based sukuk." *Butterworths Journal of International Banking and Financial Law*. 25, no. 6 (2010): 366-67.
- Ahmed, Habib. "Islamic Law, Adaptability and Financial Development ". *Islamic Economic Studies* 13, no. 2 (2006): 79.
- Ahmed, Habib "Maqasid al-Shari'ah and Islamic Financial Products: A Framework for Assessment." *ISRA International Journal of Islamic Finance* 3, no. 1 (2011): 149-60.
- Ahmed, Moinuddin. *Ulama : the Boon and Bane of Islamic Society*. New Delhi: Kitab Bhavan, 1990.
- AI-Sadah, Anwar Khalifa "Corporate Governance of Islamic Banks: Characteristics and Effects on Stakeholders and the Role of Islamic Banks Supervisors." PhD thesis, University of Surrey, School of Management, 2007.
- Ainley, Michael, A. Mashayekhi, R. Hicks, A. Rahman, and A. Ravalia. *Islamic Finance in The UK : Regulation and Challenges*. London: Financial Services Authority., 2007.
- Ajija, Shochrul Rohmatul, Mia Fathia, and Agusdiwana Suarni. *Tawarruq: Issue & Challenge*. Brunei Darussalam, 2010. http://www.researchgate.net/publication/215447064_TAWARRUQ_ISSUES_AND_CHALLENGES
- al- Āmidī, Muḥammad 'Alī. *al-Iḥkām fī Uṣūl al-Aḥkām*. edited by Sayyid al-Jamīlī. Vol. 1: Dār al-Kitāb al-'Arabī, 1984.

- al-Aghbarī, Ismā'īl. "Taqnīn al-Fiqh al-Islāmī: Qānūn al-Aḥwāl al-Shakhṣiyah al-'Umānī Unmūdhajan." Taddart, http://www.taddart.org/ar/?p=12767#_ftn18. accessed 8 October 2012
- Al-Ahmad, Hend. "al-ghāmidī: ghālibiyah al-qanawāt al-maṣrifīyah al-slāmīyah lā tuṭabq mābādī al-āqtiṣād al-slāmī." *Alsharq Newspaper* 30/1/2012.
- al-'Ajlān, 'abdAllāh. *al-Qaḍā' bi-al-Qarā'in al-Mu'āṣirh*. Jāmi'ah al-Imam Moḥammad bin Saud al-Islamiyah, 2006.
- al-'Anasy, Aḥmad Qāsim. *al-Tāj al-Mudhdhab l' Ahkām al-Madhab*. Vol. 2: Maktabah al-Yaman, 1961.
- al-'Arabī, Quṭb. "al-Baḥrayn al-Maṣārif al-Islāmiyah Tūḥḥad al-Shī'ah wā al-sunnah." Alarabiya.Net, <http://www.al-asfoor.org/?id=1002>. accessed 10 April 2012
- al-Ashqar, Osāmah. *Fawḍā al-Iftā*. Dār al-Nfā'is, 2009.
- al-'Asqalānī, Aḥmad Ibn Ḥajar. *Fath al-Bārī Sharḥ Ṣaḥīḥ al-Bukhārī*. edited by Muḥammad Fu'ād 'Abd al-Bāqī. Vol. 12: Dār al-Ma'rifah, 1963.
- al-Azdī, 'Abd al-Ghanī Sa'īd. *Kitāb al-Mutawārīn*. edited by Mashhūr Ḥasan Salmān: Dār al-Qalam 1989.
- al-Bahlāl, 'AbdAllāh Furayḥ. "al-Raqābah al-Shar'īyah Fī al-Bunūk al-Su'ūdiyyah " Master thesis Imam University, Higher Institute of Justice, 2003.
- al-Baḥrānī, Yūsuf. *al-Ḥadā'iq al-Nāḍirah fy Ahkām al-'Utrah al-Ṭāhirah*. edited by Muḥammad Taqī al-Ayrawānī. 2ed ed. Vol. 25: Dār al-Aḍwā', 1989.
- al-Bāḥsayn, Ya'qūb 'Abd al-Wahāb. *al-Takhrīj ind al-Fuqahā' w al-Aṣūliān*. Maktabah al-Rushd, 1994.
- al-Ba'ī, 'Abd āl-Ḥamid "al-Qawānīn Wa al-Tashrī'āt al-Maṣrifīyah al-Islāmiyyah Dirāsāt Muqāranah " Paper presented at the The 7th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 27/5/2008.
- al-Ba'ī, 'Abd āl-Ḥamid "al-Raqābah al-Shar'īyah al-Fa'ālah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah " Paper presented at the The Third International Conference on Islamic Economics, Umm Al Qura University, Mecca, 31/5-02/06/2005.
- al-Ba'ī, 'Abd āl-Ḥamid "Astiql-āliyyat al-Hay'ah al-Shar'īyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah " Paper presented at the The 2nd Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 29-30/10/2002.
- al-Ba'ī, 'Abd āl-Ḥamid "Tanẓīm al-'alāqah ban al-Maṣārif al-Islāmiyyah Wa al-Bunūk al-Markaziyyah Wa al-Bunūk al-Taqlīdiyyah al-Ukhrā." Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005.
- al-Balkhī, Nizām al-Dīn, and Others. *al-Fatāwā al-Hindiyyah fī Madhhab al-Imām al-A'zam abī Ḥanīfah al-Nu'mān*. Vol. 6: Dār al-Fikr, 1991.
- al-Bānī, Muḥammad Sa'īd. *'Umdah al-Taḥqīq fī al-taqlīd wa al-talfīq*. edited by Ḥasan Su'aydān. 2nd ed.: Dār al-Qādirī, 1998.
- al-Bukhārī, Muhammad Ismā'īl. "Ṣaḥīḥ al-Bukhari." Sunnah.com, <http://sunnah.com/urn/21000>. accessed 20 April 2012
- al-Bukhārī, Muhammad Ismā'īl. "Ṣaḥīḥ al-Bukhari." Sunnah.com, <http://sunnah.com/urn/65420>. accessed 1 April 2012
- al-Bukhārī, Muhammad Ismā'īl. "Ṣaḥīḥ al-Bukhārī." Sunnah.com, <http://sunnah.com/urn/49830>. accessed 4 July 2012
- al-Bukhārī, Muhammad Ismā'īl. "Ṣaḥīḥ al-Bukhārī." Sunnah.com, <http://sunnah.com/bukhari/40#12>. accessed 1 April 2012
- al-Bukhārī, Muhammad Ismā'īl. "Ṣaḥīḥ al-Bukhārī." Sunnah.com, <http://sunnah.com/urn/65530>. accessed 1 April 2012
- al-Būrnū, Muḥammad Ṣdqī. *Mawsū'ah al-Qawā'id alFfghyyh*. Vol. 1: Maktabah al-Tawbah, 2000.
- al-Būrnū, Muḥammad Ṣdqī. *Mawsū'ah al-Qawā'id alFfghyyh*. Vol. 5: Maktabah al-Tawbah, 2000.
- al-Būṭī, Muḥammad Sa'īd. *Dawābiṭ al-Maṣlaḥah fī al-Sharī'ah al-Islāmiyyah*. Mu'assisah al-Risālah, 1973.

- al-Darir, al-Saddiq Muhammad al-Amin. *Al-Gharar in contracts and its effects on contemporary transactions*. Jiddah: Islamic Research and Training Institute, 1997.
- al-Duranī, Fathī. *al-Nazariyyāt al-Fiqhīh*. 4th ed.: Jāmi'ah Dimashq, 1996.
- al-Ḍuwayhī, Ahmad. "Dawābiṭ al-Ijtihād fī al-Mu'āmalāt al-Māliyyat al-Islāmiyyah." Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, Dubai, UAE, 15-17/5/2005.
- al-Fūzān, 'Abdāl'azīz "Qā'imah al-Ashum al-Mubāḥah." The message of Islam <http://main.islammessage.com/newspage.aspx?id=9663>. accessed 28 May 2013
- al-Ghazālī, Abū Hāmid. *al-Mustaṣfā fī 'alm al-Uṣūl*. Vol. 1: al-Risālah, 1997.
- al-Ghufaylī, 'abdAllāh Manṣūr. "al-Ṣā' bayn al-Maqāyīs al-Qadīmah w al-Ḥadīthah." Ṣayd al-Fawā'id, <http://www.saaaid.net/bahoth/80.htm>. accessed 1 May 2012
- al-Ḥaddād, Aḥmad. "Ma'āyir al-Tamīz ban al-'Uqūd al-Ṣūriyyih wa al-Ḥaqīyyiqiyah." Paper presented at the The 10th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 26/5/2010.
- al-Ḥamawī, Aḥmad. *Ghamz 'Uyūn al-Baṣā'ir Sharḥ Kitāb al-'Ashbāh wa al-Nazā'ir*. Vol. 2: Dār al-Kutub al-'Ilmiyyah, 1985.
- al-Hamazānī, Muḥammad. "Ra'īs Ha'ah Shar'iyyah fī Akbar Bank Islāmī Uḥarim al-Tawaruq wa Uaṣifuh bi al-Ribā al-Mastūr." *Asharq Al-Awsat*, 14/9/2010.
- al-Ḥaṭṭāb, Muḥammad. *Mawāhib al-Jalīl sharḥ Mukhtaṣar Khalīl* Vol. 4, Beirut: Dār al-Fikr.
- al-Ḥiṣayn, 'abd al-Salām. *al-Qawā'id wa al-Dawābiṭ al-Fiqhiyyah lil-Mu'āmalāt al-Māliyyah 'ind Ibn Taymiyyah*. Vol. 2: Dār al-Ta'sīl, 2002.
- al-Hītī, 'Abd al-Razzāq Raḥīm "Athar al-Raqābah al-Shar'iyyah 'alā Ail-tizām al-Maṣārif al-Islāmiyyah bi-al-'Aḥkāmi al-Shar'iyyah " Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5/2009 - 3/6/2009.
- al-Ḥuwayfī, Hanā' "al-Tawarruq ḥaqīqatuh, Anwā'uuh." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- al-'Iṣaymī, ṣāliḥ. *al-Ashum al-Mukhtalīṭah fī Mīzān al-Sharī'h*. al-Tadmuriyyah, 2008.
- al-Islāmbūlī, Ahmad. "Dawr al-Hay'āt al-Shar'iyyah Fī Dabṭ A'māl al-Mu'asasāt al-Māliyyah al-Islāmiyyah " Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- al-Jar'ī, 'Abd al-Raḥman. "Taqnīn al-Fiqh al-Islāmī Bayn al-Māni'in Wa al-Mujīzīn." *Islam Today* (2005). <http://islamtoday.net/bohooth/artshow-86-5987.htm> accessed 15 July 2012
- al-Jaṣṣās, Aḥmad 'alī. *Aḥkāṃ al-Qur'ān*. edited by Muḥamad al-Ṣādiq Qamḥāwī. Vol. 1: Dār Iḥyā' al-Turāth al-'Arabī, 1985.
- al-Khaṭfī, 'Alī. *Asbāb Akhtil-āaf al-Fuqahā'*. 2nd ed.: Dār al-Fikr al-'Arabī, 1996.
- al-Khalīfī, Riyāḍ Muḥammad. "al-Nazariyyah al-'Āmmah Lil-hay'āt al-Shar'iyyah " Paper presented at the Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 5-6/10/2003.
- al-Khaṣṣāf, Aḥmad 'Umar. *Kitāb al-Ḥiyal*. Maṭba'ah al-Qāhirah, 1896.
- al-Khilālyh, Yḥyā. "Taqnīn al-Sharī'ah al-Islāmiyyh bayn al-Nazzrīh wa al-Tatbīq." PhD thesis International Islamic University, 2002.
- al-Khin, Muṣṭafā. *Athar al-Akhtilāaf fī al-Qawā'id al-Uṣūliyyah fī Akhtil-āaf al-Fuqahā'*. 7th ed.: Resalah Publishers, 1998.
- al-Khuwaylidī, 'Abd al-Sattār "al-Ākhtīṣās al-Qānūnī Wa al-Ḥimāyah al-Jinā'iyyah Lil-hay'āt al-Shar'iyyah " Paper presented at the Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 5-6/10/2003.
- al-Kuwaytiyyah, Wzārah al-Awqāf. *al-Mawsū'ah al-Fiqhiyyah*. Vol. 32: Wzārah al-Awqāf al-Kuwaytiyyah, 1995.
- al-Maqdisī. "Takhrij Ḥadīth lā Tartakibū mā Artakabat al-Yahūd." Multaqā Ahl al-Ḥadīth, <http://www.ahlalhaddeeth.com/vb/showthread.php?t=53252>. accessed 8 March 2012
- al-Maqdisī, 'Abd Allāh Aḥmad Ibn Qudāmah. *al-Mughnī fī Fiqh al-Imām Aḥmad Ibn Hanbal al-Shaybānī*. Vol. 4: Dār al-Fikr, 1985.
- al-Maqdisī, Abū Muḥammad 'Aṣim. *al-Kawāshif al-Jaliyyah fī Kufr al-Dawlah al-Su'ūdiyyh* Vol. 2013: al-Tawḥīd wa al-Jihād 2000.

- al-Mashūh, Khālīd "Taṭwīr Kuliyyāt al-Sharī'ah " Alwatan,
<http://www.alwatan.com.sa/Articles/Detail.aspx?ArticleId=2887>. accessed 10 July 2011
- al-Maṣrī, Rafīq Ūnis. "al-Ḥīl al-Fiqhiyyah bayn al-Būṭī wā Ibn Qaim al-Jawziyyah." Islamic Economic Research Centre,
http://islamiccenter.kau.edu.sa/arabic/Hewar_Arbeaa/abs/263/Hiwar1430-16.pdf. accessed 10 May 2012
- al-Maṣrī, Rafīq Ūnis. " al-Tawaruq fy al-Bunūk hl hū Mubāarak Am Mash'ūm " Markaz Abḥāth al-Āqtiṣād al-Islāmī
http://islamiccenter.kau.edu.sa/arabic/Hewar_Arbeaa/abs/164.htm. accessed 10 December 2013
- al-Maṣrī, Rafīq Ūnis, and Muḥammad riyāḍ al-Abrash. *al-Ribā wa al-Fā'idh : dirāsah aqtiṣādiyyah muqārinah*. Damascus: Dār al-Fikir, 2001.
- al-Maymān, Nāṣir. "al-Talfīq fī al-Ijtihād wa al-Taqlīd." *Majalh al-'adl* 3, no. 11 (2001): 1.
- al-Mīlānī, Fāḍil al-Ḥusaynī. "al-Iftirād al-Qānūnī wa al-Ḥīlah al-Shar'iyyah." Almilani,
<http://almilani.org/%D8%B9%D8%B1%D8%A8%D9%8A/%D8%A7%D9%84%D9%85%D9%82%D8%A7%D9%84%D8%A7%D8%AA/696>. accessed 18 April 2012
- al-Mirdāwī, 'Alī. *al-Inṣāf fī ma'rifah al-Rājiḥ min al-Khilāf* Vol. 11, 1956.
- Al-Mubarak, Tawfiq , and Noor Mohammad Osmani. "Applications of Maqasid al-Shari'ah and Maslahah in Islamic Banking practices: An Analysis." Paper presented at the International Seminar on Islamic Finance in India, Kochi, India, 4 - 6 /10/ 2010.
- al-Muḥaqq al-Ḥīlī. *Sharā'i' al-Islām fī Masā'il al-Ḥalāl wa al-Ḥarām*. edited by al-Sayyid ṣādiq al-Shīrāzī. Vol. 3: Intishārāt Istiql-āal, 1983.
- al-Murtaḍā, Aḥmad Yaḥyā. *al-Baḥr al-Zakhār al-Jāmi' Limadhdhāhib 'Ulamā' al-Amṣār*. Vol. 3: Dār al-Kitāb al-Islāmī, 1973.
- al-Muzaynī, Khālīd. "Tarshīd al-'Amal Fī al-Ḥa'āt al-Shar'iyyah Lil-mu'assasāt al-Māliyyah al-Islāmiyyah." Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5 - 3/6/2009.
- al-Nadawī, 'Alī Aḥmad. *Mawsū'ah al-Qawā'id wa al-Ḍawwābiṭ al-Fiqhiyyah al-Ḥākimah lil-Mu'āmalāat al-Māliyyah*. Vol. 1: Dār 'Ālm al-Ma'rifah, 1999.
- al-Najjār, 'AbdAllāh Mabruk "Muftariḍāt al-Mas'ūliyyah fī Niṭāq al-Raqābah al-Shar'iyyah 'alā al-Mu'assasāt al-Māliyyah " Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UEA, 26/4/2009.
- al-Namarī, Yūsuf Ibn 'Abd al-Bar. *Jāmi' Bayān al-'Ilm wa Faḍlih*. edited by Abī al-Ashbāl al-Zahārī. Vol. 2: Dār abn al-Jawzī, 1994.
- al-Naqīb, Aḥmad Muḥammad. *al-Madhdhab al-Ḥanaḥfī*. Vol. 1: Maktabah al-Rushd, 2001.
- al-Nasā'i, Aḥmad shu'ayb. *al-Mujtabā min al-Sunan*. edited by 'Abd al-Fattāḥ Abū Ghuddah. 2ed ed. Vol. 8: Maktab al-Maṭbū'āt al-Islāmiyyah 1986.
- al-Nasser, Lahem. "Waḍ' al-Maṣrifīyyah al-Islāmiyyah Murbik Wa Naḥn Biḥājah ilā Wilādah Jadīdah " *Islamic Finance and Investment* 01/09/2010.
- al-Nawawy, Muḥyyī al-Dīn Yaḥyā. *al-Majmū' Sharḥ al-Muhadhdhab*. edited by Muḥammad Najīb al-Muṭī'ī. Vol. 9: Maktabah al-Irshād, 1971.
- al-Nawawy, Muḥyyī al-Dīn Yaḥyā. *Rawḍah al-Ṭālibīn wa 'Umdah al-Muftīn*. edited by Zuhayr al-Shāwīsh. Vol. 3: al-maktab al-islāmī, 1385.
- al-Naysaburi, Muslim ibn al-Hajjaj "Sahih Muslim." Sunnah.com,
<http://sunnah.com/muslim/22/132>. accessed 10 January 2014
- al-Othaimeen, Mohammad. "al-Taḥdhīr min al-Fatawā bighar 'ilm, al-Taḥdhīr min Kutmān al-'ilm." Ibnnothaimeen.com,
http://www.ibnothaimeen.com/all/khotab/article_121.shtml. accessed 23 July 2013
- Al-Qara Daghi , Ali. " Murāj'at Fatāwā Nadwat al-Barakah. ." <http://www.isra.my/media-centre/downloads.html?task=finish&cid=102&catid=21>. accessed 10 November 2013
- al-Qarāfī, Aḥmad Idrīs. *al-furūq*. edited by Khalīl al-Manṣūr. Vol. 2: Dār al-Kutub al-'ilmiyyah, 1998.
- al-Qarḍāwī, Yūsuf. *Sharī'ah al-Islām Ṣāliḥ lil-Taṭbīq fī Kul Zamān w Makān*. 2ed ed.: Dār al-Ṣaḥwah, 1993.

- al-Qaṭṭān, ‘Abd al-Sattār. "Sharikāt al-Āsitishārāt al-Shar‘iyyah: al-ausus wa al-ḍawābiṭ w al-mutaṭallabāt." Paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 18-19/5/2009.
- al-Qaṭṭān , ‘Abd al-Sattār ‘Alī "Madā Ta‘āruḍ al-Maṣāliḥ Fī A‘māl Hay’āt al-Riqābah al-Shar‘iyyah." Paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 18-19/5/2009.
- al-Qurashī, ‘AbdAllāh Marzūq. *Ishkāliyyh al-Ḥiyal fī al-Baḥṭh al-Fiqhī*. Namaa for Research and Studies Centre, 2012.
- al-Raḥman, al-‘irāqī zan al-Dīn ‘abd. *Ṭarḥ al-Tathrīb fī Sharḥ al-Taqrīb*. edited by Aḥmad ‘Abd al-Raḥīm Abū Zar‘ah. Vol. 2: Dār Iḥyā’ al-Turuāth al-‘arabī, 1934.
- al-Rā‘ī, Sulaymān Na‘īm "Athar Hay’āt al-Fatwā wa al-Riqābah al-Shar‘iyyah Fī al-Mu‘asasāt al-Māliyyah al-Islāmiyyah " Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005.
- al-Rīsūnī, Quṭb "Naḥw Ta‘hīl Ajtihādī Li’A‘ḍā’ Hay’ah al-Fatwā bi-al-Maṣārif al-Islāmiyyah." Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5 - 3/6/2009.
- al-Rustāqī, Muḥamad. *al-Qadīm wa al-Jadīd Min Madhhab al-Imām al-Shāfi‘ī*. Dār Ibn Ḥazm 2005.
- al-Sa‘ad, Ahmad Muḥammad "al-Raqābah al-Shar‘iyyah Wa’ Atharhā Fī al-Maṣārif al-Islāmiyyah." Paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/06/2005.
- al-Saati, Abdurrahim "The Permissible Gharar (Risk) in Classical Islamic Jurisprudence ". *Islamic Economics* 16, no. 2 (2003): 3.
- al-Sa‘īdī, ‘abdAllāh. "Madhāhib al-Fuqahā’ fī al-‘īnah." *al-Dr‘iyyh* 7, no. 26 (2004): 59.
- al-Sa‘īdī , ‘AbdAllāh "al-Tawaruq kamā tujrīh al-Maṣārif fī al-Waqt al-ḥāḍir ". *Majalah al-Mjama’ al-Fiqh al-Islāmi*, no. 18 (2004): 197.
- al-Sa‘īdī, Muḥammad "Qirā’ah Shar‘iyyih fī al-Nizām al-Asāsī Lil-ḥukum." Lojainiat, <http://lojainiat.com/main/Content/%D9%82%D8%B1%D8%A7%D8%A1%D8%A9-%D8%B4%D8%B1%D8%B9%D9%8A%D8%A9-%D9%81%D9%8A-%D8%A7%D9%84%D9%86%D8%B8%D8%A7%D9%85-%D8%A7%D9%84%D8%A3%D8%B3%D8%A7%D8%B3%D9%8A-%D9%84%D9%84%D8%AD%D9%83%D9%85-%D9%81%D9%8A-%D8%A7%D9%84%D9%85%D9%85%D9%84%D9%83%D8%A9-%D8%A7%D9%84%D8%B9%D8%B1%D8%A8%D9%8A%D8%A9-%D8%A7%D9%84%D8%B3%D8%B9%D9%88%D8%AF%D9%8A>. accessed 10 May 2013
- al-Sakrān, Ibrāhīm. *al-Ashum al-Mukhtanliṭah*. Wahaj al-ḥayāh Lil-‘lām, 2005.
- al-Ṣalāḥīn, ‘Abd al-Majīd Maḥmūd "Hay’āt al-Fatwā Wa al-Riqābah al-Shar‘iyyah Wa Dawruhā Fī al-Maṣrifīyyah al-Islāmiyyah " Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15-17/5/2005.
- al-Ṣāliḥ, Muḥammad Aḥmad. "Dawr al-Raqābah al-Shar‘iyyah Fī Ḍabṭ a‘māl al-Maṣārif al-Islāmiyyah " Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- al-Sālūs , ‘Alī. "al-‘īnah wa al-Tawaruq wa al-Tawarruq al-Maṣrifī." Paper presented at the The 17th session of the International Islamic Fiqh Academ, Makkah, 13- 17 /12/2003.
- al-Sanhūrī, Abd al-Razzāq. *Maṣādir al-Ḥaq fī al-Fiqh al-Islāmī*. Vol. 4, Cairo: Jāmi‘ah al-Duwal al-‘Arabīh 1967.
- al-Saud, Abdalaziz Ibn Sṭtam. "Siyāsah al-Jawdah al-Shar‘iyyah fī al-Maṣrifīyaah al-Islāmiyyah." *al-Fiqh al-Islāmī* (2011). <http://www.islamfeqh.com/News/NewsItem.aspx?NewsItemID=4004> accessed 10 May 2012
- al-Sawādī, ‘Amrū. "Da‘awāt Ijād Muntajāt Islāmiyyah lil-Ta‘āmul ma‘ al-Qurūḍ al-Muta‘athrih." *al-Iqtiṣādiyaah*, 22 May 2011.

- Al-Sayari, Hamad. "Saudi Arabian Banking System & Capital Markets." SAMA, <http://www.sama.gov.sa/sites/samaen/News/Pages/News14230708.aspx>. accessed 10 May 2013
- al-Sayyid, Riḍwān. "al-Fiqh wa al-Siyāsah fī al-Tajrubah al-Islāmiyyah al-Wasīṭah." *Majalah al-Tafāhum*, no. 25 (2009): 209-333.
- al-Shabīlī, Yūsuf ‘AbdAllāh. "al-Raqābah al-Shar‘iyyah ‘Alā al-Maṣārif: Dawābiḥā Wa Ahkāmḥā Wa Dawrhā fī Dabṭ ‘Amal al-Maṣārif." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- al-Shabīlī, Yūsuf ‘AbdAllāh. "Qā’imah al-Ashum al-Jā’izah " Shubily, <http://www.shubily.com/index.php?news=348>. accessed 10 May 2013
- al-Shāfi‘ī, al-Bayān fī Madhhab al-Imām. *al-Umrānī, Yahyā*. edited by Qāsim Muḥammad al-Nūrī. Vol. 5: Dār al-Minhāj, 2000.
- al-Shāfi‘ī, Muḥammad Idrīs *al-Umm*. edited by Muḥammad Zuhri al-Najār. Vol. 3: Mmaktabah al-Kullīāt al-Azhariyah, 1961.
- al-Sharīf, Muḥammad ‘Abd al-Ghaffār "al-Raqābah al-Shar‘iyyah ‘Alā al-Mu’assasāt al-Tamwīliyyah al-Islāmiyyah." Paper presented at the TheThird International Conference on Islamic Economics, Mecca, Mecca, 31/5-2/6/2005.
- al-Shāṭibī, Ibrāhīm Mūsā. *al-Ā’iṣām*. edited by Salīm ‘Id al-Hilālī. Vol. 1: Dār Ibn ‘Afān, 1992.
- al-Shāṭibī, Ibrāhīm Mūsā. *al-Muwāfaqāt*. edited by Mashhūr Ḥasan Salmān. Vol. 2: Dār Ibn ‘Affān, 1997.
- al-Shāṭibī, Ibrāhīm Mūsā. *al-Muwāfaqāt*. edited by Mashhūr Ḥasan Salmān. Vol. 1: Dār Ibn ‘Affān, 1997.
- al-Shāṭibī, Ibrāhīm Mūsā. *al-Muwāfaqāt*. edited by Mashhūr Ḥasan Salmān. Vol. 5: Dār Ibn ‘Affān, 1997.
- al-Shāṭibī, Ibrāhīm Mūsā. *al-Muwāfaqāt*. edited by Mashhūr Ḥasan Salmān. Vol. 3: Dār Ibn ‘Affān, 1997.
- al-Shaybāny, Muḥammad Ibn al-Ḥasan. *al-Makhārij fī al-Ḥiyal*. Maktabah al-Thaqāfah al-Dīnīh, 1999.
- Al-Suwailem , Sami. "Tawarruq Banking Products." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- Al-Suwailem, Sami. "Towards An Objective Measure of Gharar in Exchange." *Islamic Economic Studies* 7, no. 1 (2000): 61-102.
- al-Tamīmi, ‘Abū al-‘Arb Muḥammad Aḥmad. *Kitāb al-Miḥan*. edited by Yahyā Wahyb al-Jabbwry. 3ed ed.: Dār al-Gharb al-Islāmī, 2006.
- al-Ṭayyib, ‘Abd al-Mun‘im Muḥammad "Taḥqīm al-Raqābah al-Shar‘iyyah fī Zil al-Nizām al-Maṣrifī al-Islāmī al-Shāmil." Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5- 3/6/2009.
- al-Ṭūfī, Sulamān ‘Abd al-Qawī. *Sharḥ Mukhtaṣar al-Rawḍah*. edited by ‘AbdAllāh ‘Abd al-Muḥsin al-Turkī. Vol. 3: Mu’sasah al-Risāl, 1987.
- al-Turkī, ‘AbdAllāh. *Asbāb Akhtil-āaf al-Fuqahā’*. 3rd ed.: Resalah Publishers, 2010.
- al-‘Ukbarī, Ibn Batah. *Ibṭāl al-Ḥiyal*. edited by Sulaymān al-‘Umayr: Al-Resalah 1996.
- al-Wad‘ānnī, Ḥusayn. "al-Manī‘ antaqid "sāmā" wa uṭālibuhā bi" Maṣrifīyyih Islāmiyyih " Alwatan Online http://www.alwatan.com.sa/Economy/News_Detail.aspx?ArticleID=30871&CategoryID=2. accessed 10 May 2013
- al-Zarqā, Muḥammad Anas Muṣṭafā. "al-Haykal al-Shar‘ī Lil-ṣṣinā‘at al-Māliyyah al-Islāmiyyah Jawānib al-Khalal wa Ṭarīq al-Ṣlāh " Paper presented at the Symposium on Values and Morals For Tthe Work of Economic Institutions, Kuwait 30/3/2008.
- al-Zarqā, Muṣṭafā. *al-Fiqh al-Islāmī Wa Madārisah*. Dār al-Qalam, 1995.
- al-Zarqā, Muṣṭafā. *al-Madkhal al-Fiqhī al-‘ām*. Vol. 1: Dār al-Qalam, 1998.
- al-Zuhaylī, Wahbah. *al-Fiqh al-Islāmī wa Adilatuh* 4th ed. Vol. 4: Dār al-Fikr, 1997.
- al-Zuhaylī, Wahbah. *Financial Transactions in Islamic Jurisprudence*. Translated by El-Gamal Mahmoud A. and Eissa Muhammad S. Vol. 1, Damascus, Syria: Dar al-Fikr, 2007.

- Al Arabiya News. "Saudi king limits clerics allowed to issue fatwas." Alarabiya.net, <http://www.alarabiya.net/articles/2010/08/12/116450.html>. accessed 8 September
- Alarabiya. "halaqah zayd akhū 'ubayd fī tash 18 takshif wasā'il al-bunūk al-islāmiyah fī al-tahāul biālibā." Alarabiya.net, <http://www.alarabiya.net/articles/2011/08/11/161888.html>. accessed 21 April 2012
- Albahooth, Abdullah. *al-Tawarruq al-Maṣrifī al-Munazm wa āthāruh al-āqtiṣādiyah*. Riyadh: Dār Kunūz Ashbīliyā, 2011.
- Aldeen, Abdulmomen Shuja'a. "Mawqif al-Fuqahā' min Taqnīn Aḥkām al-Sharī'ah al-Islāmiyah." *Organization House of Law*. <http://ohlyemen.org/modules.php?name=News&file=article&sid=110> accessed 10 June 2012
- Aldohni, Abdul Karim. "Islamic Banking Challenges Modern Corporate Governance: The Dilemma of The Shari'a Supervisory Board." *Company Lawyer* 29, no. 5 (2008): 156-60.
- Aldohni, Abdul Karim. *The Legal and Regulatory Aspects of Islamic Banking : a Comparative Look at The United Kingdom and Malaysia*. London: Routledge, 2011.
- Aleshaikh, Nourah "Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place." Durham University, 2011.
- Ali, Abdullah Yusuf. *The Holy Qur'an :Text, Translation and Commentary*. Brentwood, Md.: Amana Corp., 1983.
- Ali, Shaheen Sardar, and Musa Usman Abubakar. "Part 1: Islamic Finance Techniques: the Sunni schools' differing approaches." *Butterworths Journal Of International Banking & Financial Law* 25, no. 5 (2010): 308-11.
- Alinma Bank. "Annual Report 2010." Alinma Bank,, http://www.alinma.com/wps/wcm/connect/512dd680467a8afb930ebb690642abc7/Alinma_annual_report_2010_eng%28may22%29+22.5.11.pdf?MOD=AJPERES&CACHEID=512dd680467a8afb930ebb690642abc7. accessed 28 August 2011
- Alinma Bank. "Shariah Board." http://www.alinma.com/wps/portal/alinma/!ut/p/c5/04_SB8K8xLLM9MSSzPy8xBz9CP0os3hzf2cLDy93A0t3d1c3A093Ixd3_yBfI29TA_3g1Dz9gmxHRQA7laOC/. accessed 28 August 2011
- Alkhamees, Ahmad. "The Impact of Shari'ah Governance Practices on Shari'ah Compliance in Contemporary Islamic Finance." *Journal of Banking Regulation* 14, no. 2 (10 September 2012 2012): 134-63.
- Alkhamees, Ahmad. "International Arbitration and Shari'a Law: Context, Scope, and Intersections." *Journal of International Arbitration* 28, no. 3 (2011): 255-64.
- Alrajhi Bank. "2009 Annual Report." Alrajhi Bank, <http://www.alrajhibank.com.sa/reports/Pages/default.aspx>. accessed 10 March 2011
- Alrajhi Bank. "About Us." <http://www.alrajhibank.com.sa/AboutUs/Pages/default.aspx>. accessed 18 April 2011
- Alrajhi Bank. "Annual Report 2010." Alrajhi Bank, <http://www.alrajhibank.com.sa/en/media-centre/reports/Documents/annual-report2010-en.pdf>. accessed 28 August 2011
- Alrajhi Bank. "The Sharia Group." <http://www.alrajhibank.com.jo/AboutUs/Pages/ShariaaGroup.aspx>. accessed 10 December 2010
- Alsayed, Nidal. "Shari'ah Board, The Task of Fatwa, and Ijtihad in Islamic Economics, and Finance." *MPRA Paper* (2009). <http://mpra.ub.uni-muenchen.de/20204/> accessed 22 October 2010
- AlShalhoob, Salah. "Organised Tawarruq in Islamic Law: a Study of Organised Tawarruq as Practised in the Financial Institutions in Saudi Arabia." Paper presented at the IIUM International Conference on Islamic Banking and Finance, Kuala Lumpur 23-25/4/2007.
- Amīn, Aḥmad. *Duḥā al-Islām*. Vol. 2: al-Hay'ah al-'Āmah al-Maṣrīh lil-Kitāb, 1998.

- Ammari, Siba Sami. "Islamic Finance Industry Exceeds Growth Expectation as Conventional Finance Suffers through Economic Crisis." AME Info FZ LLC / Emap Limited, <http://www.ameinfo.com/218528.html>. accessed 12 September 2011
- Ansari, Omar Mustafa "Roles and responsibilities of shariah advisors in Islamic banking institutions." *True Banking*, 42-44.
- Antonio, Muhammad Syafii "What is the Future Outlook of Shar'iah Harmonization?" Paper presented at the (ISRA) Islamic Finance Seminar, Kuala Lumpur, 11/11/2008.
- Arab National Bank (ANB). "al-Tawarruq al-Mubark." ANB, http://www.anb.com.sa/arabic/loan_tawarruq_local.asp. accessed 10 December 2013
- Arab National Bank (ANB). "Annual Report." http://www.anb.com.sa/pdf/Reports/2010/ANB_English_review.pdf. accessed 28 August 2011
- Arab National Bank (ANB). "Islamic Banking Division Profile." http://www.anb.com.sa/about_islamic.asp. accessed 28 August 2011
- Asutay, Mehmet. "Conceptualisation of the Second Best Solution in Overcoming the Social Failure of Islamic Finance: Examining the Overpowering of Homoislamicus by Homoeconomicus." *IUM Journal of Economics and Management* 15, no. 2 (2007): 167-95.
- Aṭfaysh, Muḥammad Yūsuf *Sharḥ al-Nīl wa Shifā' al-'Alīl*. Vol. 8: Maktabah al-Irshād, 1985.
- Athar, Osama. "An Outsider's View on Islamic Finance", Harvard Islamic Finance Forum". Dinar Standard™, <http://www.dinarstandard.com/finance/HarvardFin051908.htm>. accessed 10 November 2011
- Attia, Gamal Eldin. *Towards Realization of the Higher Intents of Islamic law : Maqasid al-Shari'ah : a functional approach*. Translated by Nancy Roberts. London [etc.]: International Institute of Islamic Thought, 2007.
- Auda, Jasser. *Maqasid al-Shariah as Philosophy of Islamic Law: a Systems Approach*. London: International Institute of Islamic Thought, 2008.
- Ayub, Muhammad. *Understanding Islamic Finance*. Hoboken, NJ: John Wiley & Sons, 2007.
- Bā'alawī, 'abd āl-Raḥman Muḥammad. *Bughyah al-Mustarshidīn*. Dār al-Fikr, 2001.
- Baamir, Abdulrahman, and Ilias Bantekas. "Saudi Law as Lex Arbitri: Evaluation of Saudi Arbitration Law and Judicial Practice." *Arbitration International* 25, no. 2 (2009): 239-69.
- Bacha, Obiyathulla I. "Dual Banking Systems and Interest Rate Risk for Islamic Banks." *The Journal of Accounting, Commerce & Finance* 8, no. 1 (2004): 1-42.
- Bahjat, Muḥammad Fu'ād. "Naḥw Mi'yār Lil-rriqābah al-Shar'īyyah Fī al-Bunūk al-Islāmiyyah." *Journal of King Abdulaziz University: Islamic Economics* 3, no. 2 (1994).
- Bakar, Mohd Daud. "Conflict of Law and The Methodology of Tarjih: a Study in Islamic Legal Theory." PhD thesis, University of St. Andrews, 1993.
- Bakar, Mohd Daud. "The Shari'a Supervisory Board and Issues of Shari'a Rulings and their Harmonisation in Islamic Banking and Finance." In *Islamic Finance: Innovation and Growth*, edited by Simon Archer and Rifaat Ahmed Abdel Karim, 74-89. London: Euromoney Books and AAOIFI, 2002
- Bakr, Zayn Ibn Ibrāhīm *al-Baḥar al-Rā'iq* Vol. 6, Beirut Dār al-Ma'rifh.
- Bälz, Kilian. "A Murabaha Transaction in An English Court - The London High Court of 13th February 2002 in Islamic Investment Company of the Gulf (Bahamas) Ltd. V. Symphony Gems N.V. & Ors." *Islamic Law and Society* 11, no. 1 (2004): 117-34.
- Bank Albilad. "Financial Statements for 2010." <http://www.bankalbilad.com/en/BILAD31-12-2010.pdf>. accessed 28 August 2011
- Bank Albilad. "Sharia Board." <http://www.bankalbilad.com/ar/shariah.asp>, <http://www.bankalbilad.com/en/shariah.asp>. accessed 28 August 2011

- Bank AlJazira (BAJ). "Annual Report." <http://www.baj.com.sa/pdf/Baj%20Annual%20Report%20English.pdf>. accessed 28 August 2011
- Bank AlJazira (BAJ). "Corporate Profile." <http://www.baj.com.sa/about-us.aspx?page=corporate-profile&id=139>. accessed 28 August 2011
- Bank Negara Malaysia (BNM). "Profile of current SAC members (2010 - 2013)." BNM,, <http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802>. accessed 16 May 2013
- Bank Negara Malaysia (BNM). "Shari'ah Governance Framework for Islamic Financial Institutions (BNM/RH/GL_012_3)." Bank Negara Malaysia, http://www.bnm.gov.my/guidelines/05_shariah/02_Shariah_Governance_Framework_20101026.pdf. accessed 11 December 2010
- Bank Negara Malaysia (BNM). "Shariah Scholarship Award." Bank Negara Malaysia, <http://www.bnm.gov.my/index.php?ch=200&pg=618&ac=529>. accessed 20 May 2011
- Bank Saudi Fransi (BSF). "Annual Report." <http://www.alfransi.com.sa/en/general/download/file/1369>. accessed 28 August 2011
- Bank Saudi Fransi (BSF). "Islamic Finance " <http://www.alfransi.com.sa/en/article/corporate-services/corporate-banking/islamic-finance.html>. accessed 28 August 2011
- Bāryān, ‘Ādil ‘AbdAllāh "Asālīb Taf’īl Dawr al-Raqābah al-Shar‘iyyah Fī al-Maṣārif al-Islāmiyyah " Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5- 3/6/2009.
- Bean, Gerard M. D. *Fiduciary Obligations and Joint Ventures :The Collaborative Fiduciary Relationship*. Oxford; New York, N.Y.: Clarendon Press, 1995.
- Bedoui, Houssemeddine, and Walid Mansour. "Islamic banks performance and Maqasid alShari’ah." Paper presented at the the 9th Asia-Pacific Economic Association Conference, Osaka, Japan, 27-28/7/2013.
- Belder, Richard de. "Form Over Substance – Will the Secular Courts Force the Issue?" *Newhorizon*, 2011, 27-29.
- Berhad, Syarikat Takaful Malaysia. "Glossary of Takaful." <http://www.takaful-malaysia.com.my/corporate/takafuloverview/pages/glossarytakaful.aspx>. accessed 11 April 2014
- Bewley, Aisha "The 'Amal of Madina." www.bewley.virtualave.net, <http://bewley.virtualave.net/amalmadina.html>. accessed 10 August 2012
- Bi, Farmida. "AAOIFI Statement on Sukuk and its Implications." Norton Rose Fulbright, <http://www.nortonrosefulbright.com/knowledge/publications/16852/aoifi-statement-on-sukuk-and-its-implications>. accessed 20 May 2013
- Bill, Maurer. "Form Versus Substance: AAOIFI Projects and Islamic Fundamentals in the Case of Sukuk." *Journal of Islamic Accounting and Business Research* 1, no. 1 (2010): 32-41.
- Boucek, Christopher "Saudi Fatwa Restrictions and the State-Clerical Relationship." Carnegie Endowment for International Peace, <http://www.carnegieendowment.org/sada/?fa=aboutSada>. accessed 12 September 2012
- Bruce, Martha. *Rights and Duties of Directors*. London: Tolley Publishing Co Ltd, 2002.
- "Capital Market Law." Royal Decree No. (M/30), <http://www.cma.org.sa/En/AboutCMA/CMALaw/Documents/CAPITAL%20MARKET%20LAW-26-8-009.pdf>. accessed 25/09/2011
- "CBK Law No. (32) of 1968." CBK http://www.cbk.gov.kw/www/law_iii.html#ch3_10. accessed 8 September 2011
- Chapra, M. Umer. "The Case Against Interest: Is It Compelling?". *Thunderbird International Business Review* 49, no. 2 (2007): 166-86.
- Chapra, M. Umer, and Habib Ahmed. *Corporate Governance in Islamic Financial Institutions*. Jeddah: Islamic Development Bank, 2002.
- Clarke, Thomas. *International Corporate Governance : a Comparative Approach*. London [u.a]: Routledge, 2007.

- CME Group Index Services. "Guide to the Dow Jones Islamic Market Indexes." CME Group Index Services, accessed 15 May 2013
- Commissions, Executive Committee of The International Organization Of Securities. "Analysis of The Application of IOSCO's Objectives And Principles of Securities Regulation For Islamic Securities Products " International Organization of Securities Commissions (IOSCO) <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD280.pdf>. accessed 17 June 2012
- Cook, M. A. *Commanding Right and Forbidding Wrong in Islamic Thought*. Cambridge, UK; New York: Cambridge University Press, 2000.
- Coulson, Noel J. *A History of Islamic Law*. Edinburgh: Edinburgh University Press, 2003.
- Dabu, Ibrahim Fadhil. "Tawarruq, Its Reality and Types." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- Dal Bó, Ernesto. "Regulatory Capture: A Review." *Oxford Review of Economic Policy* 22, no. 2 (Summer 2006): 203-25.
- Dar, Humayon. "Implementing Shari'ah Governance -Awaiting Challenges." Paper presented at the Managing Shariah Risk through Shariah Governance, London, 10/8/2009.
- Dar, Humayon A., and John R. Presley. "Lack of Profit Loss Sharing in Islamic Banking: Management and Control Imbalances." *International Journal of Islamic Financial Services* 2, no. 2 (2000): 3-18.
- Davies, Paul L. *Introduction to Company Law*. Oxford: Oxford University Press, 2010.
- Dawud, Abu. "Sunan Abi Dawud: Knowledge (Kitab Al-Ilm)." Sunnah.com, <http://sunnah.com/abudawud/26/18>. accessed 19 May 2013
- DeLorenzo, Yusuf Talal. "The Black Box Syndrome: A New Challenge for Shariah Supervisory Boards." Islamic Finance news, <http://www.shariahunds.com/pubs/news/Islamic%20Finance%20News%20V4i14.pdf>. accessed 11 March 2014
- DeLorenzo, Yusuf Talal. "Shari'ah Compliance Risk." *Chicago Journal of International Law* 7, no. 2 (2007): 397-408.
- DeLorenzo, Yusuf Talal. "Shari'ah Supervision in Modern Islamic Finance." <http://www.nzibo.com/IB2/Shari'ahsupervision.pdf>. accessed 8 February 2011
- Djojosingito, Reza. "Mitigating Legal Risk in Islamic Banking Operations." *Humanomics* 24, no. 2 (2008): 110-21.
- Dobinson, Ian, and Francis Johns;. "Qualitative Legal Research." In *Research Methods for Law*, edited by Wing McConville Mike Hong Chui. Edinburgh: Edinburgh Univ. Press, 2007
- Dubai Islamic Bank (DIB). "Hay'ah al-Fatwā Wa al-Raqābah al-Shari'iyah " DIB,, <http://www.dib.ae/ar/shariaboard.htm>. accessed 29 April 2011
- Dusuki, Asyraf Wajdi. *Can Bursa Malaysia Suq al-Sila' (Commodity Murabahah House) Resolve the Controversy over Tawarruq?* Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2010.
- Dusuki, Asyraf Wajdi, and Said Bouheraoua. *The Framework of Maqasid Al-Shari'ah (Objectives of the Shari'ah) And Its Implications in Islamic Finance*. Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA),, 2011.
- Eddy Yusof, Ezry Fahmy , Jhordy Kashoogie, and Asim Anwar Kamal. "Islamic Finance: Debt versus Equity Financing in the Light of Maqasid al-Shari'ah.", (2009). <http://mpira.ub.uni-muenchen.de/id/eprint/20722> accessed 10 February 2014
- Editorial. "Shariah Auditing for the Islamic Finance Industry." *Islamic Finance News* 9th November 2011, 1.
- El-Gamal, Mahmoud Amin. *A Basic Guide to Contemporary Islamic Banking and Finance*. Houston, TX: Rice University, 2000.
- El-Gamal, Mahmoud Amin. *Islamic Finance : Law, Economics, and Practice*. Cambridge UK: Cambridge University Press, 2006.
- El-Hawary, Dahlia, Wafik M. Graiss, and Zamir Iqbal. "Regulating Islamic Financial Institutions : The Nature of The Regulated." *World Bank Policy Research Working Paper* 3227, March 2004 (2004). <http://www->

- wds.worldbank.org/external/default/WDSContentServer/TW3P/IB/2004/06/03/000009486_20040603173425/additional/112512322_20041117151025.pdf accessed 10 December 2010
- El Baltaji, Dana, and Haris Anwar. "Shariah Scholar on More Than 50 Boards Opposes Limit Plan: Islamic Finance." Bloomberg, <http://www.bloomberg.com/news/2010-11-23/shariah-scholar-on-more-than-50-boards-opposes-limit-plan-islamic-finance.html>. accessed 25 November 2010
- El Diwany, Tarek, ed. *Islamic Banking and Finance : What it is and What it could be*. Bolton: 1st Ethical Charitable Trust, 2010.
- El Diwany, Tarek. *The Problem With Interest*. 3d ed. London: Kreatoc, 2003.
- Elgari, Mohamed. "al-Tawarruq Kamā tujrīh al-Maṣārif " Paper presented at the 17th session of the Islamic Fiqh Academy, Makkah, 13-17/12/2003.
- Ercanbrack, Jonathan. "The Regulation of Islamic Finance in the United Kingdom." *Ecclesiastical Law Journal* 13, no. 1 (2011): 69-77.
- European Islamic Investment Bank plc's (EIIB). "Annual Report " EIIB,, <http://www.eiib.co.uk/documents/EIIBAnnualReport2010Final.pdf>. accessed 28 August 2011
- European Islamic Investment Bank plc's (EIIB). "Sharia Board." EIIB,, http://www.eiib.co.uk/html/sharia_board.asp. accessed 28 August 2011
- Executive Committee of IOSCO. "Analysis of The Application of IOSCO's Objectives And Principles of Securities Regulation For Islamic Securities Products " International Organization of Securities Commissions (IOSCO),, <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD280.pdf>. accessed 17 June 2012
- Fahmy, E, F Faisal, A Habshi, W Hassan, F Ariffin, K Kuan, and Y Azizakhon. "Revisiting OIC Fiqh Academy Rules on Organised Tawarruq." (2008). <http://www.scribd.com/doc/21445765/Revisiting-OIC-Fiqh-Academy-Rules-on-Organised-Tawarruq> accessed 10 November 2013
- Fahmy, Ezry. "Shari'ah Scholars as an Independent Director: A Proposal." *Shirkah* 16-17.
- Farah, Fayṣal 'Abd al-'Azīz. "al-Raqābah al-Shar'īyyah al-Wāqī' Wa al-Mithāl " Paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/06/2005.
- Farber, Daniel A. "Taking Slippage Seriously: Noncompliance and Creative Compliance in Environmental Law." *Harvard Environmental Law Review* 23, no. 2 (1999): 297-326.
- Fāris, Ṭah Muḥammad. "Dawābiṭ Wa Āliyyāt Akhtiyār A'dā' Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Fī al-Mu'asasāt al-Māliyyah " Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31/5- 3/6/2009.
- Fayyād, 'Aṭīyyah "al-Raqābah al-Shar'īyyah Wa al-Taḥaddiyāt al-Mu'āṣirah " Paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/6/2005.
- "Federal Law No-(6) of 1985 concerning Islamic Banks and Financial Institutions and Investment Companies." Central Bank of United Arab Emirates <http://www.centralbank.ae/pdf/LawNo6-1985-IslaminBanks.pdf>. accessed 10 November 2011
- Fidād, al-'Yāashyi al-Ṣādiq. "al-Raqābah al-Shar'īyyah Wa Dawruhā Fī Dabṭ A'māl al-Maṣārif al-Islāmiyyah." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/4/2009.
- Fidād, al-'Yāashyi al-Ṣādiq. "Ta'arūḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'īyyah " Paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, Bahrain, 18-19/5/2009.
- Filimbān, Ḥassān. *Khabar al-Wāḥid Idhā Khālaf 'Amal ahl al-Madīnah*. Dār al-Buḥūth lil-Dirāsāt al-Islāmiyyah Wa Iḥyā al-Turāth, 2000.
- Financial Conduct Authority (FCA). "Combined Initial Disclosure Document " FCA,, http://www.fca.org.uk/static/fca/documents/handbook/cobs6_annex2_20130401.doc. accessed 1 March 2014

- Financial Conduct Authority (FCA). "The Fit and Proper test for Approved Persons." FCA, <http://media.fshandbook.info/content/FCA/FIT.pdf>. accessed 4 April 2014
- Financial Conduct Authority (FCA). "Principles for Businesses." FCA,, <http://media.fshandbook.info/content/full/PRIN/2/1.pdf>. accessed 10 May 2013
- Financial Conduct Authority (FCA). "What is an approved person?" FCA, <http://www.fca.org.uk/firms/being-regulated/approved/approved-persons>. accessed 4 April 2014
- Financial Services Authority. "Approved persons." FSA,, <http://www.fsa.gov.uk/Pages/Doing/Regulated/Approved/persons/index.shtml>. accessed 24 December 2011
- Financial Services Authority. "Conduct of Business Sourcebook (COBS)." FSA,, <http://fshandbook.info/FS/html/handbook/COBS/4/2>. accessed 10 May 2013
- Financial Services Authority. "Financial Services Authority Annual Report 2011/12." FSA,, <http://www.fsa.gov.uk/pubs/annual/ar11-12/ar11-12.pdf>. accessed 19 May 2013
- Financial Services Authority. "FSA advises industry on definition of "mis-selling"." FSA,, <http://www.fsa.gov.uk/library/communication/pr/2003/052.shtml>. accessed 9 May 2013
- Financial Services Authority. "Mortgage Market Review (Conduct Of Business) Instrument 2012." FSA,, http://media.fshandbook.info/Legislation/2012/2012_46.pdf. accessed 10 May 2013
- Financial Times Lexicon. "Unsolicited Rating." Financial Times,, <http://lexicon.ft.com/Term?term=unsolicited-rating>. accessed 18 May 2013
- Firoozye, Nikan. "Tawarruq: Shariah Risk or Banking Conundrum?" Opalesque Islamic Finance Intelligence, http://www.opalesque.com/OIFI12/Featured_Structure_Tawarruq_Shariah_Risk_or_Banking438.html. accessed 09 December 2010
- Firoozye, Nikan. "Wa'd and the completeness of Islamic markets." Opalesque Islamic Finance Intelligence, <http://www.kantakji.com/media/7540/c69.pdf>. accessed 5 May 2013
- Foot, Michael. "The Future of Islamic Banking in Europe." FSA, <http://www.fsa.gov.uk/library/communication/speeches/2003/sp150.shtml>. accessed 10 May 2013
- Foster, Nicholas H. D. "Islamic Finance Law as an Emergent Legal System." *Arab Law Quarterly* 21, no. 2 (2007): 170-88.
- FTSE Group. "FTSE Shariah Global Equity Index Series." FTSE,, http://www.ftse.co.uk/Indices/FTSE_Shariah_Global_Equity_Index_Series/index.jsp. accessed 22 May 2013
- Garas, Samy Nathan , and Chris Pierce. "Shari'a Supervision of Islamic Financial Institutions." *Journal of Financial Regulation and Compliance* 18, no. 4 (2010): 386-407.
- Gatehouse Bank. "Annual Report." http://www.gatehousebank.com/common/documents/annual-reports/Gatehouse_Bank_Annual_Report_2009.pdf. accessed 28 August 2011
- Gatehouse Bank. "Shariah Supervisory Board." <http://www.gatehousebank.com/about-us/shariah-supervisory-board/>. accessed 28 August 2011
- Ghazzali. *The Book of Knowledge; Ihya`ulum al-din*. . Translated by Nabih Amin Faris. 2nd ed. Lahore: S.M. Ashraf, 1966.
- Ghoul, Wafica Ali "Shariah Scholars and Islamic Finance: Towards a more Objective and Independent Shariah-Compliance Certification of Islamic Financial Products." *Review of Islamic Economics* 12, no. 2 (2008): 87-104.
- Ghoul, Wafica Ali "The Standardization Debate in Islamic Finance: A Case Study " Paper presented at the 8th International Conference on Islamic Economics and Finance, Doha, 18/12/2011.

- Gietzmann, Miles B., and Pradyot K. Sen. "Improving Auditor Independence Through Selective Mandatory Rotation." *International Journal of Auditing* 6, no. 2 (2002): 183–210.
- Goldziher, Ignác *Introduction to Islamic Theology and Law*. Translated by Andras Hamori and Ruth Hamori. Princeton, N.J.: Princeton University Press, 1981.
- Goldziher, Ignaz. *The Zahiris: Their Doctrine and Their History*. Translated by Wolfgang Behn. edited by Wolfgang Behn Leiden; Boston: Brill, 2008.
- Goolam, Nazeem MI. "Ijtihad and Its Significance for Islamic Legal Interpretation ". *Michigan State Law Review* 2006, no. 6 (2006): 1443.
- Goud, Blake. "Bahrain's Central Banker Supports Making IFSB Standards Mandatory." *Sharing Risk*, <http://investhalal.blogspot.co.uk/2013/01/bahrains-central-banker-supports-making.html>. accessed 25 May 2013
- Grais, Wafik, and Matteo Pellegrini. "Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services." *World Bank Policy Research Working Paper 4054* (2006). <http://ssrn.com/abstract=940711> accessed 2 December 2010
- Guo, Li *The Performing Arts in Medieval Islam*. Leiden; Boston: Brill, 2012.
- H. M. Treasury. "The Development of Islamic Finance in the UK the Government's perspective." HM Treasury, http://webarchive.nationalarchives.gov.uk/20120306210332/http://www.hm-treasury.gov.uk/d/islamic_finance101208.pdf. accessed 10 May 2013
- Ḥabtūr, ‘Abd al-Hādī. "Hay’āt Riqābiyyah Shar‘iyyah fī al-Mašārif al-Islāmiyyah Ta‘mal k " Muassasāt Khayriyyat " Dūn Šifah Qānūniyyah " *al-Āqtišādiyyah*, 20 June 2010.
- Ḥabtūr, ‘Abd al-Hādī. "Mukhtašūn: al-Bunūk al-Islāmiyyah tastakhdim al-Tawarruq fī dārah al-Suūlah rughm al-Taḥafuzāt al-Shar‘iyyah." *al-Āqtišādiyyah*, 8 January 2012.
- Hainsworth, Antony. *Islamic financial institutions and islamic finance*. London: LexisNexis, 2009.
- Hallaq, Wael B. *A History of Islamic Legal Theories: An Introduction to Sunni Usul al-Fiqh*. Cambridge, UK: Cambridge University Press, 1997.
- Hallaq, Wael B. *An introduction to Islamic law*. Cambridge, UK; New York: Cambridge University Press, 2009.
- Hallaq, Wael B. *The Origins and Evolution of Islamic Law*. Cambridge, UK: Cambridge University Press, 2005.
- Hallaq, Wael B. "Was the Gate of Ijtihad Closed?". *International Journal of Middle East Studies* 16, no. 1 (1984): 3-41.
- Ḥamād, ‘adlī. "Da‘wah Lījād Marjī ‘iyyah Shar‘iyyah Rasmiyaah Lisūq al-Māl Wālmašārif." *Okaz*, 19/8/2010.
- Hamdan, Sara. "Non-Sharia Compliance Costs sSukuk Industry Billions." *The National*, <http://www.zawya.com/Story.cfm/sidZAWYA20090414051357/Non-Sharia%20Compliance%20Costs%20Sukuk%20Industry%20Billions>. accessed 6 October 2010
- Ḥamīsh, ‘Abd al-Ḥaq "Hay’ah al-Fatwā Wa al-Raqābah al-Shar‘iyyah Fī al-Mašārif al-Islāmiyyah " Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15/5/2005.
- Hammad, Ahmad Zaki. *Islamic Law: Understanding Juristic Differences*. Indianapolis: American Trust Publications, 1992.
- Ḥammād, Ḥamzah ‘Abd al-Karīm. *al-Raqābah al-Shar‘iyyah Fī al-Mašārif al-Islāmiyyah* Amman: Alinvaais, 2006.
- Hamoudi, Haider Ala. "Jurisprudential Schizophrenia: On Form and Function in Islamic Finance." *Chicago Journal of International Law* 7, no. 2 (2007): 605.
- Haneef, Rafe. *Is the Ban on "Organised Tawarruq" the Tip of the Iceberg?* Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2009.
- Hasan, Aznan. "Optimal Shari’ah Governance in Islamic Finance." *BNM*, http://www.bnm.gov.my/microsites/giff2007/pdf/frf/04_01.pdf. accessed 17 October 2010

- Hasan, Zubair. "Fifty Years of Malaysian Economic Development: Policies and Achievements." *Review of Islamic Economics* 11, no. 2 (2007): 101-18.
- Hasan, Zubair. "Islamic Finance: The Structure-Objective Mismatch and its Consequences." *ISRA International Journal of Islamic Finance* 2, no. 1 (2010): 35-60.
- Hasan, Zulkifli. "Demystifying The Myth Of Shortage Of Shari'ah Scholars." *Global Islamic Finance Magazine*, 66-68.
- Hasan, Zulkifli. "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK." *Kyoto Bulletin of Islamic Area Studies on Islamic Finance* 3, no. 2 (2010): 82-115.
- Hasan, Zulkifli. "Shari'ah Governance in Islamic Financial Institutions in Malaysia, GCC countries and the UK." PhD thesis University of Durham, School of Government and International Affairs, 2011.
- Hassan, Hussain Hamed. *Nazarīh al-Maṣlahah f al-Fiqh al-Islāmī*. Maktabah al-Mutanabī, 1981.
- Hassan, Hussain Hamed "al-‘Alāqah Bayn al-Hay’āt al-Shar‘iyyah wa al-murāji‘īn al-khārijiyyīn " Paper presented at the The First Conference for Shari'a Supervisory Boards, Bahrain, 9/10/2001.
- Hassan, Rusni , Uzaimah Ibrahim, Nurdianawati Irwani Abdullah, Akhtarzait Abd Aziz, and Mohd. Fuad Sawari. *An Analysis of the Role and Competency of the Shari'ah Committees (SCs) of Islamic Banks and Financial Service Providers* Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance ISRA 2010.
- Hatina, Meir. *Guardians of Faith in Modern Times : `Ulama in The Middle East*. Boston: Brill, 2009.
- Hegaz, Walid. "Fatwas and the Fate of Islamic Finance: A Critique of the Practice of Fatwa in Contemporary Islamic Financial Markets ". In *Islamic Finance: Current Legal and Regulatory Issues*, edited by Nazim Ali: Islamic Finance Project, Islamic Studies Program, Harvard Law School., 2005
- Henderson, Andrew. "Islamic Financial Institutions." In *Islamic Finance: Law and Practice*, edited by Craig Nethercott and David Eisenberg. Oxford Oxford University Press, 2012
- Hennigan, Peter C. "Ahl al-ra'y." In *Encyclopaedia of Islam*: Brill, 2012
<http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-3/ahl-al-ray-COM_22177> accessed 1 April 2012
- Hermalin, Benjamin E., and Michael S. Weisbach. "Transparency and Corporate Governance." (2007). http://www.law.yale.edu/documents/pdf/cbl/HW_mkts_v5.pdf accessed 28 August 2011
- Hilali, Taqi al-Din, and Muhammad Muhsin Khan. "The Noble Quran." Muslim Directory, <http://quran.com/5/6>. accessed 2 July 2012
- Hilali, Taqi al-Din, and Muhammad Muhsin Khan. "The Noble Quran." Muslim Directory, <http://quran.com/35/28>. accessed 7 August 2011
- Hilali, Taqi al-Din, and Muhammad Muhsin Khan. "The Noble Quran." Muslim Directory, <http://quran.com/65/4>. accessed 4 July 2012
- Hilali, Taqi al-Din, and Muhammad Muhsin Khan. "The Noble Quran." Muslim Directory, <http://quran.com/2/282>. accessed 15 October 2012
- Hirschman, Albert O. *Exit, Voice, and Loyalty; Responses to Decline in Firms, Organizations, and States*. Cambridge, Mass.: Harvard University Press, 1970.
- Hmīṣah, Badr ‘Abd al-Ḥamīd "Muḥāsabah al-Wulāh " Ṣayd al-Fawā'id
<http://www.saaaid.net/Doat/hamesabadr/205.htm>. accessed 9 August 2011
- Holmes, Zeynep, and Surinder Kathpalia. "Standard & Poor's Islamic Finance Outlook 2014."
http://www.standardandpoors.com/spf/upload/Ratings_EMEA/IslamicFinanceOutlook_2014.pdf. accessed 6 March 2014
- Howladar, Khalid. "The Future of Sukuk: Substance over Form?" Moody's Investors Service, <http://www.kantakji.com/fiqh/Files/Markets/m170.pdf>. accessed 30 October 2012

- Howladar, Khalid. "Shari'ah Risk: Understanding Recent Compliance Issues in Islamic Finance." Moody's, http://eng.assaif.org/content/download/7643/43051/file/MDYs_ShariahRisk_KHowladar.pdf, accessed 17 October 2010
- Hsayn, Muḥammad al-Khiḍr. *al-Sharī'ah ṣāliḥh likul Zamān wa Makān*. edited by Muḥammad 'Imārah: Nahḍah Maṣr, 1999.
- HSBC Amanah. "Shariah Supervision." <http://www.hsbcamanah.com/amanah/about-amanah/islamic-banking/shariah-supervision>, accessed 28 August 2011
- Hussainey, Khaled, and Ali Al-Nodel. "Corporate Governance Online Reporting by Saudi Listed Companies." In *Corporate governance in less developed and emerging economies*, edited by Matthew Tsamenyi and Shazad Uddin, 39-64. Bingley: Emerald Jai, 2008
- Ibn 'Ashur, Muḥammad al-Tahir *Ibn Ashur : treatise on Maqasid al-Ahari'ah*. Herndon, VA.: International Institute of Islamic Thought, 2006.
- Ibn 'ābidīn, Muḥammad Amīn *Raddu al-Muḥtār 'Alā al-Durri al-Mukhtār sharḥ Tanwīr al-Absār*. edited by 'Ādil 'Abd al-Mawjūd and 'Alī 'Awaḍ. Vol. 4: Dār al-Kutub al-'Ilmīyah, 2003.
- Ibn al-Qayyim, Muḥammad bn Abī Bakr. *I'lām al-Mawqī 'ayn 'an Rab al-'Ālamīn*. edited by Ṭah 'Abd al-Ra'uf Sa'd. Vol. 3: Dār al-Jil, 1973.
- Ibn al-Qayyim, Muḥammad bn Abī Bakr. *Tahdhīb Sunan Abī Dāwd*. Vol. 5, Makkah: Dar al-baz, 1980.
- Ibn al-Qayyim, Muḥammad Ibn Abī Bakr. *al-Ṭuruq al-Ḥukmiyyah fī al-Siyāsīh al-Shar'īyah*. edited by Nāyif al-Ḥamad: Dār 'ālam al-Fawā'id, 2007.
- Ibn Bayyah, 'AbdAllāh. *Sadd al-Dharī'ah wa Taṭṭbīqātuh fī Majāl al-Mu'āmalāt*. Islamic Development Bank, 1997.
- Ibn Ḥazm, 'Alī Aḥmad. *al-Muḥallā bi-al-'Āthār*. edited by 'Abd al-Ghaffār Sulaymān al-Bnadārī. Vol. 7: Dār al-Fikr, 1988.
- Ibn Ḥazm, 'Alī Aḥmad. *al-Muḥallā bi-al-'Āthār*. edited by 'Abd al-Ghaffār Sulaymān al-Bnadārī. Vol. 12: Dār al-Fikr, 1988.
- Ibn Ḥumayd, Ahmad 'AbdAllāh. "Dawr al-Raqābah al-Shar'īyyah Fī Dabṭ a'māl al-Maṣārīf al-Islāmiyyah." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UAE, 26/9/2009.
- Ibn Kathir, Ismail ibn Umar. "Tafsir Ibn Kathir " Darussalam, http://www.qtafsir.com/index.php?option=com_content&task=view&id=1906&Itemid=, accessed 8 August 2011
- Ibn Khuldūn, 'Abd al-Raḥman. *Tārīkh Ibn Khuldūn*. edited by Khalīl Shahādah. Vol. 1: Dār al-Fikr, 2001.
- Ibn Nujaym, Zayn al-'ābidīn Ibrāhīm. *al-'ashbāh wa al-nazā'ir*. edited by Muḥammad Muṭī' al-Ḥāfīz. 2nd ed.: Dār al-Fikr, 2005.
- Ibn Rushd, Abu al-Walīd Muḥammad. *al-Bayān wa al-Taḥṣīl wa al-Shirḥ wa al-Tawjīh wa al-Ta'līl limasā'il al-Mustakhrajah*. edited by Muḥammad Ḥijy. 2ed ed. Vol. 18: Dār al-Gharb al-Islāmī, 1988.
- Ibn Rushd, Abu al-Walīd Muḥammad. *Bidāyah al-Mujtahid w Nihāyah al-Muqtaṣid* edited by Abd Allāh al-'Abādī. Vol. 3: Dār al-Salāam, 1995.
- Ibn Taymiyah, Aḥmad. *Raf' al-Malāam 'an al-'Imah al-'Alāam*. The General Presidency of Scholarly Research and Ifta, 1993.
- Ibn Taymiyah, Aḥmad ibn 'Abd al-Ḥalīm. *al-Fatāwā al-Kubrā*. edited by Muḥammad 'atā and 'abd al-Qādir 'atā. Vol. 6: Dār al-Kutub al-'ilmīyyh, 1987.
- Ibn Taymiyah, Aḥmad ibn 'Abd al-Ḥalīm. *al-Qawā'id al-Nawrānīh al-Fiqhiyah*. edited by Muḥammad Ḥāmid al-Faqī: Maktabah al-Sunnah al-Muḥammadiyyh, 1951.
- Ibn Taymiyah, Aḥmad ibn 'Abd al-Ḥalīm. *Bayān al-Dalīl 'alā Ibṭāl al-Taḥlīl*. edited by Ḥamdī 'Abd al-Majīd al-Salafī: al-Maktab al-Islāmī, 1988.
- Ibn Taymiyah, Aḥmad ibn 'Abd al-Ḥalīm. *Majmū' Fatāwā Shaykh al-Islām Ibn Taymiyah*. edited by Abd al-Raḥman Ibn Qāsim. Vol. 20: Mujamma' al-Malik Fahd liṭibā'at al-Muṣhaf al-Sharīf, 2004.

- Ibn Taymiyah, Ahmad ibn 'Abd al-Halim. *Majmū' Fatāwā Shaykh al-Islām Ibn Taymiyah*. edited by Abd al-Rahman Ibn Qasim. Vol. 29: Mujamma' al-Malik Fahd liṭibā'at al-Muṣḥaf al-Sharīf, 2004.
- Ibrāhīm, Muḥammad. *al-Ḥiyal al-Fiqhiyyah fī al-Mu'āmalāt al-Māliyyah*. Dar Alsalam, 2008.
- Institute of Islamic Banking and Insurance (IIBI). "3rd Annual ISRA/IIBI Thematic Workshop: Monday, 12th December 2011." http://www.islamic-banking.com/resources/1/Workshops%202011/IIBI-ISRA%20SNR%20DENTON%20WS%202011%20ver%204_invite%20reduce%20only.pdf. accessed 10 May 2012
- Institute of Islamic Banking and Islamic Insurance(IIBI). "About Us." IIBI,, <http://www.islamic-banking.com/about.aspx>. accessed 23 May 2011
- Investment Dar Co KSCC v Blom Developments Bank Sal*, [2009] EWHC 3545 (Ch) (2009).
- Iqbal, Munawar, and David T. Llewellyn eds. *Islamic Banking and Finance : New Perspectives on Profit Sharing and Risk*. Cheltenham, UK; Northampton, MA: Edward Elgar in association with International Association of Islamic Economics, Islamic Development Bank [and] The Islamic Foundation.
- Iqbal, Zafar, and Mervyn Lewis. *An Islamic Perspective on Governance*. Cheltenham, U.K.; Northampton, Mass.: Edward Elgar, 2009.
- 'Isā, Mūsā Ādam. "Ta'āruḍ al-Maṣāliḥ Fī A'māl Hay'āt al-Riqābah al-Shar'īyyah." Paper presented at the The 8th Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 18/5/2009.
- 'Isā, Mūsā Ādam. " Taṭbīqāt al-Tawaruq wa Astikhḍāmātuh fī al-'amal al-Maṣrifī al-Islāmī " Paper presented at the Dawr al-Mu'sasāt al-Maṣrifīyah fī al-āstithmār wa al-Tanmiyyah, Sharjah, UAE, 7-9 /5/2002.
- Islamic Bank of Britain (IBB). "Sharia Supervisory Committee." <http://www.islamic-bank.com/sharia-finance/sharia-supervisory-committee/>. accessed 28 August 2011
- Islamic Bank of Britain IIBI. "Annual Report and Financial Statements " <http://www.islamic-bank.com/GetAsset.aspx?id=fAAzADkANgB8AHwAVABvAHUAZQB8AHwAMA B8AA2>. accessed 28 August 2011
- Islamic Finance Council UK (IFC), and International Shari'ah Research Academy for Islamic Finance (ISRA). "Enhancing Shari'ah Assurance." IFC,, <http://www.ukifc.com/ifc-isra-launch-pioneering-shariah-assurance-report>. accessed 16 May 2013
- Islamic Finance News. "Shariah Auditing for the Islamic Finance Industry." *Islamic Finance News*,, 9th November 2011, 1.
- Islamic Financial Services Board (IFSB). "Background." IFSB,, <http://www.ifsb.org/background.php>. accessed 20 May 2013
- Islamic Financial Services Board (IFSB). "Disclosures to Promote Transparency and Market Discipline for Institutions offering Islamic Financial Services." IFSB,, <http://www.ifsb.org/standard/ifsb4.pdf>. accessed 19 May 2013
- Islamic Financial Services Board (IFSB). "Guiding Principles on Conduct of Business for Institutions offering Islamic Financial Services (IFSP-9) " IFSB,, http://www.ifsb.org/standard/IFSB-9_Guiding%20Principles%20on%20Conduct%20of%20Business.pdf. accessed 28 May 2013
- Islamic Financial Services Board (IFSB). "Guiding Principles on Shariah Governance Systems for Institutions Offering Islamic Financial Services." IFSB,, <http://www.ifsb.org/standard/IFSB-10%20Shariah%20Governance.pdf>. accessed 29 March 2011
- Islamic International Rating Agency (IIRA). "Corporate Profile." IIRA, <http://www.iirating.com/CoperateProfile.aspx>. accessed 10 May 2013
- Islamic International Rating Agency (IIRA). "IIRA withdraws AA (SQR) rating assigned to Syarikat Takaful Malaysia Berhad " IIRA, http://www.iirating.com/Documents/PressReleasePdf/SQR_withdrawal_of_Syarikat_TM.pdf. accessed 11 May 2013

- Islamic International Rating Agency (IIRA). "Methodology for Shari'ah Quality Rating." IIRA, http://www.iirating.com/Documents/ResearchReports/sharia_methd_eng.pdf. accessed 10 May 2013
- Islamic International Rating Agency (IIRA). "Press Releases." IIRA, <http://www.iirating.com/ResourceCenterNavigation.aspx>. accessed 12 May 2013
- Islamic International Rating Agency (IIRA). "Rating." IIRA, <http://www.iirating.com/RatingNavigations.aspx>. accessed 13 May 2013
- Ismail, Muhammad "'Substance' over 'Form' in Islamic Finance: Analysis of Murabaha and Ijara Contracts." Newhorizon, <http://www.newhorizon-islamicbanking.com/index.cfm?section=iibinews&action=view&id=10825>. accessed 30 October 2012
- Issa, Nabil A "Beyond Tawarruq: Availability of Other Forms of Islamic Financing in Saudi Arabia." Islamicfinancenews.com, <http://www.kslaw.com/imageserver/KSPublic/library/publication/IslamicFinanceNewsNabilIssaOct2010.pdf>. accessed 20 June 2012
- Jadwa. "Launch of the Russell-Jadwa Shariah Indexes." Jadwa <http://www.jadwa.com/en/news/news/news-2009/launch-of-the-russell-jadwa-shariah-indexes.html>. accessed 22 May 2013
- Jamieson, Neil, and Kelly Hughes. "The Identification of Shadow Directors under English law: what guidance might Buzzle provide?". *Butterworths Journal of International Banking and Financial law*. 27, no. 6 (2012): 364-66.
- Jordan. "Law No. 28 of 2000." Jordan central bank http://www.cbj.gov.jo/pages.php?menu_id=123&local_type=0&local_id=0&local_details=0&local_details1=0&localsite_branchname=CBJ. accessed 11 September 2011
- Kahf, Monzer. "Maqasid al Shari'ah in the Prohibition of Riba and their Implications for Modern Islamic Finance." Paper presented at the IIUM International Conference on Maqasid al Shari'ah, Kuala Lumpur, Malaysia, 8-10/8/2006.
- Kahf, Monzer. "Outlines Of a Brief Framework of Tawarruq (Cash Procurement) And Securitization In Shariah and Islamic Banking ", (2004). http://monzer.kahf.com/papers/english/a_brief_framework_of_Tawarruq_AND_SECURITIZATION.pdf accessed 10 November 2013
- Kamali, Mohammad Hashim. "Al-Maqasid Al-Shari'ah: The Objectives Of Islamic Law." *The Muslim Lawyer Journal* 3, no. 1 (1998): 1-7.
- Kamali, Mohammad Hashim. *Principles of Islamic Jurisprudence*. Third ed. Cambridge, UK: Islamic Texts Society, 2003.
- Kamali, Mohammad Hashim. "Shari'ah and Civil Law: Towards a Methodology of Harmonization." *Islamic Law and Society* 14, no. 3 (2007): 391.
- Kechichian, Joseph A. "The Role of the Ulama in the Politics of an Islamic State: The Case of Saudi Arabia." *International Journal of Middle East Studies* 18, no. 1 (1986): 53-71.
- Khan, Feisal. "How 'Islamic' is Islamic Banking?". *Journal of Economic Behavior & Organization* 76, no. 3 (2010): 805-20.
- Khan, M. Fahim. "Setting Standards for Shariah Application in The Islamic Financial Industry." *Thunderbird International Business Review* 49, no. 3 (2007): 285-307.
- Khan, M. Fahim, and Mario Porzio. *Islamic Banking and Finance in the European Union: A Challenge*. Edward Elgar Ltd, 2010.
- Khan, M. Mansoor, and M. Ishaq Bhatti. "Islamic Banking and Finance: On Its Way to Globalization." *Managerial Finance* 34, no. 10 (2008): 708-25.
- Khan, Mir Siadat Ali. "The Mohammedan Laws against Usury and How They Are Evaded." *Journal of Comparative Legislation and International Law* 11, no. 4 (1929): 233-44.
- Khan, Muhammad Akram. *Islamic Economics and Finance : a Glossary*. London; New York: Routledge, 2003.
- Khan, Salman. "Why Tawarruq Needs To Go? AOIFI and the OIC Fiqh Academy: Divergence or Agreement?" Institute of Islamic Banking and Insurance, [302](http://www.newhorizon-</p>
</div>
<div data-bbox=)

- islamicbanking.com/index.cfm?section=academicarticle&action=view&id=10735. accessed 18 May 2013
- Khniifer, Mohammed. "\$ 31 Billion evaporate in 2008 after Osmani's Statements and the Financial Crisis." *Alaqtadyh Newspaper*, 17 January 2009.
- Khniifer, Mohammed. "Ya 'qūbī li "ālāqtiṣādiyāh": Lam Atahadda Majma' al-Fiqh Bifatwā al-Tawarq wa 'alā al-Fuqahā' al-Tafrīq bana «al-Munḍabiṭ» wa«ghari al-Munḍabiṭ»." *Alaqtadyh*, 52/07/2010.
- Khorshid, Aly "Shariah Board Accountability." Academy UK, <http://www.academyuk.org/publications/view.aspx?id=19>. accessed 10 December 2010
- Krawietz, Birgit. "Cut and Paste in Legal Rules: Designing Islamic Norms with Talfiq." *Die Welt des Islams* 42, no. 1 (2002): 3-40.
- Kunhibava, S. , and Rachagan S. "Shariah and Law in Relation to Islamic Banking and Finance." *Banking and Finance Law Review* 26, no. 3 (2011): 539-54.
- Kutty, Faisal. "The Shari'a Factor in International Commercial Arbitration." *Loyola of Los Angeles international & comparative law review Loyola of Los Angeles International & Comparative Law Review* 28, no. 2 (2006): 565-624.
- Kuwait. "Central Bank of Kuwait Law No. 30/2003 " CBK,, http://www.cbk.gov.kw/www/law_iii.html#ch3_10. accessed 8 September 2011
- Laldin, Mohamad Akram. "Dawr al-Raqābah al-Shar'iyah Fī Ḍabṭ a' māl al-Maṣārif al-Islāmiyyah." Paper presented at the 19th session of the Islamic Fiqh Academy, Sharjah, UEA, 26/4/2009.
- Laldin, Mohamad Akram, and Hafas Furqani. *Developing Islamic Finance in the Framework of Maqasid al-Shari'ah: Understanding the ends (maqasid) and the means (wasa'il)*. Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA), 2012.
- Lebanon. "Law No 575 dated February 11, 2004 The Establishment of Islamic Banks in Lebanon." Banque du Liban http://www.bdl.gov.lb/circ/lawpdf/Law575_en.pdf. accessed 24 September 2011
- Lewis, Mervyn K. "Accountability and Islam." *Fourth International Conference on Accounting and Finance* (2006). <http://www.unisa.edu.au/commerce/docs/Accountability%20and%20Islam.pdf> accessed 25 July 2011
- Linant de Bellefonds, Y. "Istishāb ". In *Encyclopaedia of Islam*: Brill Online, 2012 <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/istishab-SIM_3692> accessed 10 September 2012
- Lloyds TSB. "Islamic Business Bank Account." <http://www.lloydstsbbusiness.com/accounts/islamic.asp>. accessed 28 August 2011
- Lords, Parliament House of. "Financial Services Bill : Explanatory Notes." TSO, <http://www.publications.parliament.uk/pa/bills/cbill/2010-2012/0278/en/2012278en.pdf>. accessed 25 May 2013
- Lowry, Joseph E. "The First Islamic Legal Theory: Ibn al-Muqaffa' on Interpretation, Authority, and the Structure of the Law." *Journal of the American Oriental Society* 128, no. 1 (2008): 25.
- MacKenzie, John M. *Orientalism : History, Theory, and the Arts*. Manchester; New York: Manchester University Press, 1995.
- Mahddī, Wā'il. "Ṣāliḥ Kāmil: Aghlab Muntajāt al-Bunūk al-Islāmiyyah Ghayr Islāmiyyah." ArabianBusiness.com <http://www.arabianbusiness.com/arabic/517729>. accessed 10 November 2010
- Mahdi, Wael. "Most of Islamic Financial Products are not Islamic." ArabianBusiness.com <http://www.arabianbusiness.com/arabic/517729>. accessed 10 November 2010
- Mahmood, Rafel. "Islamic Governance, Capital Structure, and Equity Finance: Examining the Possibilities of American Financial Shari'ah Boards." *International Journal of Legal Information* 37, no. 1 (2009): 29-58.

- Malaysia. "(ACT 701) Central Bank of Malaysia Act " Bank Negara Malaysia,,
http://www.bnm.gov.my/documents/act/cba2009_01.pdf. accessed 4 April 2011
- Malaysia. "Capital Markets and Services Act 2007 (CMSA)." Securities Commission,,
<http://www.sc.com.my/eng/html/cmsa/cmsa2007/cmsa2007.pdf>. accessed 29 May 2013
- Malaysia. "Civil Law Act 67 (1956),." The Commissioner of Law Revision, Malaysia,
<http://www.agc.gov.my/Akta/Vol.%202/Act%2067.pdf>. accessed 10 May 2013
- Malaysia. "Securities Commission Act 498 (1993)." Securities Commission
<http://www.sc.com.my/eng/html/resources/guidelines/SCA2005.pdf>. accessed 10 May 2013
- Mallin, Christine A. *Corporate Governance*. Oxford; New York: Oxford University Press, 2010.
- Mansoori, Muhammad Tahir "Use of Ḥiyal in Islamic Finance and its Sharī'ah Legitimacy." *Journal of Islamic Business and Management* 1, no. 1 (2011): 69.
- Mashal, Abdulbari. "al-'Affāq al-Mustaqbaliyyah Lil-rriqābah al-Shar'iyah Ru'yah Lil-ttaṭwīr " Paper presented at the About The Future of Islamic Finance: Exploring The Opportunities of Tomorrow, Kuala Lumpur, 25-27/10/2010.
- Mashal, Abdulbari. "al-Raqābah al-Shar'iyah Ilimaṣrif al-Markazī 'alā al-Mu'sasāt al-Māliyyah al-Islāmiyyh." Paper presented at the Islamic Financial Institutions: Reality Features and Future Prospects, UAE, 15/5/2005.
- Mashal, Abdulbari. "Dawr al-Ma'āyir al-Shar'iyah Wa al-Muḥāsabiyyah Fī Tanzīm al-Maṣrifīyyah al-Islāmiyyah " Paper presented at the The 2nd Conference of Islamic Financial Services, Tripoli-Libya, 27-28/4/2010.
- Mashal, Abdulbari. "khuṣūṣiyyah wa Mutataḷabāt al-Raqābah al-Shar'iyah lil-Maṣarif al-Markazī 'alā al-Mu'asasāt al-Māliyyah al-Islāmiyyah." Paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, Bahrain, 27 - 28/5/2008.
- Mashal, Abdulbari. "Sharikāt al-Āsitishārāt al-Shar'iyah wa Hay'āt al-Raqābah al-Shar'iyah: al-ḍawābiṭ wāl'āliyāt " Paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, 27 - 28/5/2008.
- Masud, Muhammad Khalid. "Ikhtilaf al-Fuqaha: Diversity in "Fiqh" as a Social Construction." *Musawah*, <http://www.musawah.org/sites/default/files/WANTED-EN-2edition.pdf>. accessed 10 October 2012
- McBarnet, Doreen J. *Crime, Compliance and Control*. Aldershot: Ashgate/Dartmouth, 2004.
- McBarnet, Doreen, and Christopher Whelan. "The Elusive Spirit of the Law: Formalism and the Struggle for Legal Control." *The Modern Law Review* 54, no. 6 (1991): 848-73.
- McCarthy, Callum. "FSA encourages growth of Islamic finance in the UK." FSA,
<http://www.fsa.gov.uk/library/communication/pr/2007/121.shtml>. accessed 10 May 2013
- Mikail, Sa'id Adekunle, and Mahamad Arifin. "A Critical Study on Shari'Ah Compliant and Shari'Ah Based Products in Islamic Banking Institutions." *Journal of Islamic and Human Advanced Research* 3, no. 4 (2013): 168-89.
- Moghul, Umar F, and Arshad A Ahmed. "Contractual Forms in Islamic Finance Law and Islamic Inv. Co. of the Gulf (Bahamas) Ltd. v. Symphony Gems N.V. & Ors.: A First Impression of Islamic Finance." *Fordham International Law Journal* 27, no. 1 (2003): 150-94.
- Mohammad, Mustafa Omar, and Syahidawati Shahwan. "The Objective of Islamic Economic and Islamic Banking in Light of Maqasid Al-Shariah: A Critical Review." *Middle East Journal of Scientific Research* 13 (2013): 75-84.
- Mohsin, Magda Ismail Abdel. "The Practice of Islamic Banking System in Sudan." *Journal of Economic Cooperation* 26, no. 4 (2005): 27-50.
- Mokhtar, Mohd Syazwan Rahimy Mohd. "Malaysia Honours Shaikh Saleh Abdullah Kamel." *Vocus*, <http://www.prweb.com/releases/2010/11/prweb4727694.htm>. accessed 23 September 2011

- Monetary and Credit Council [MCC]. "Admission Rules of SSB of Islamic Banks Operating in The Syrian Arab Republic 404, MN, B4."
<http://www.banquecentrale.gov.sy/mone-poli-ar/cmcc/cmcc-0292-ar.pdf>. accessed 09/09/2011
- Morck, Randall, and Lloyd Steier. *The Global History of Corporate Governance : an Introduction*. Cambridge, Mass.: National Bureau of Economic Research, 2005.
- Mudawi, Al Bagkir Yousif "Organization in Islamic Banking." *Journal of IB&F* 1[2], no. 2 (1984).
- Muṣṭafā, Ibrāhīm Muṣṭafā. "Taqyīm Zāhirah Taḥawul al-Bunūk al-Taqlīdiyyah Lil-maṣrifīyyat al-Islāmiyyah Dirāsah Taṭbīqiyyah ‘an Tajribah Ba‘d al-Bunūk al-Su‘ūdiyyah " Master thesis, American Open University 2006.
- Nair, Inesh, and Saleh al-Shaibany. "Oman Opens Door to Islamic Banks to curb Fund Outflows." Reuters, <http://uk.reuters.com/article/2011/05/03/oman-banks-idUKLDE7420I720110503?feedType=RSS&feedName=rbssFinancialServicesAndRealEstateNews>. accessed 30 April 2012
- Naji, Limin. *Daḥḍ Maqālah Ta‘thunr Fiqh al-Imām al-Shāfi‘ī bi-āl-Bī‘ih al-Maṣriyyh*. al-Mansurah: Dar al-Kalimah, 2012.
- Nethercott, Craig, and David Eisenberg. *Islamic Finance: Law and practice*. Oxford: Oxford University Press, 2012.
- Office of the Comptroller of the Currency (OCC). "Interpretive Letter #867." OCC,, <http://www.occ.gov/static/interpretations-and-precedents/nov99/int867.pdf>. accessed 1 May 2014
- OIC Fiqh Academy. "Resolution 179 (19/5)."
<http://www.kantakji.com/fiqh/Files/Fatawa/w246.pdf>. accessed 10 May 2013
- Oman. "Islamic Banking Regulatory Framework " The Central Bank of Oman (CBO),, <http://www.cbo-oman.org/news/IBRF.pdf>. accessed 20 May 2013
- Opalesque. "Discussion Board: Country versus Bank Shariah Boards." Opalesque, <http://www.opalesque.com/OIFI112/Discussion Board Country versus Boards579.html>. accessed 10 December 2012
- Oxford Analytica. "Islamic Finance Moves Toward Common Standards." Oxford Analytica, http://www.forbes.com/2010/03/08/islam-finance-sharia-business-oxford-analytica_2.html. accessed 23 May 2012
- Paret, R. "Istiḥsān and Istiṣlāh ". In *Encyclopaedia of Islam*: Brill Online, 2012
 <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/istihsan-and-istislah-COM_0395> accessed 10 October 2012
- Parker, Mushtak "Islamic Banking Special Supplement: Shariah Governance a Challenge to Islamic Banking." Arab News, <http://archive.arabnews.com/?page=9§ion=0&article=127292&d=11&m=10&y=2009>. accessed 15 October 2010
- Parkinson, Giles "Faith in The System." Intheblack, http://findarticles.com/p/articles/mi_qa5393/is_200708/ai_n21294575/ accessed 16 March 2011
- Pasha, Shaheen. "Investment Dar gets Sharia Board blow to Blom Case." Arabian Business, <http://www.arabianbusiness.com/investment-dar-gets-sharia-board-blow-blom-case-282707.html>. accessed 14 July 2011
- Pasha, Shaheen. "Sharia Boards face Scrutiny amid Financial Crisis." Reuters, <http://www.reuters.com/article/2010/03/11/islamic-scholars-idUSLDE62A0J420100311>. accessed 10 December 2010
- Pearce, Robert A., John Stevens, and Warren Barr. *The Law of Trusts and Equitable Obligations*. Oxford; New York: Oxford University Press, 2010.
- Philips, Abu Ameenah Bilaal. *Evolution of Fiqh : Islamic Law and the Madh-habs*. edited by Bradley Philips. 3rd ed. Riyadh: International Islamic Publishing House, 2006.
- Poon, Winnie P. H. Chan Kam C. "Solicited and Unsolicited Credit Ratings : a Global Perspective." Asian Development Bank Inst., <http://www.adbi.org/working->

- paper/2010/08/24/4048.solicited.unsolicited.credit.ratings.global/. accessed 11 May 2013
- Porter, Brenda, David J. Hatherly, and Jon Simon. *Principles of External Auditing*. Chichester, England: John Wiley, 2008.
- Powers, Paul R. *Intent in Islamic Law : Motive and Meaning in Medieval Sunni Fiqh*. Leiden; Boston: Brill, 2006.
- Pyman, Amanda. "Creative Compliance in Labour Relations: 'Turning the Law on its Head' ." In *Advances in Industrial & Labor Relations*, edited by David Lewin and Bruce E. Kaufman, 67-99: Emerald Group Publishing Limited, 2005
- Qatar Central Bank (QCB). "Instructions to Banks." Qatar Central Bank, Eleventh Edition, March, http://www.qcb.gov.qa/English/Legislation/Documents/instructionsMar09_Eng/SEVEN.pdf. accessed 29 April 2011
- Qatar Financial Centre Regulatory Authority (QFC). "Islamic Finance Rulebook (ISFI)." Qatar Financial Centre (QFC), http://www.complinet.com/net_file_store/new_rulebooks/q/f/QFCRA_1935.pdf. accessed 29 April 2011
- Qaṭṭān, Muḥammad Amīn 'Alī. "Hay'ah al-Raqābah al-Shar'iyah Akhtiyār A'ḍā'ihā Wa Dawābiḥā " Paper presented at the The Seventh Conference of the Shariah Boards of Islamic Financial Institutions, Bahrain, 27-28/5/2008.
- Qaṭṭān, Muḥammad Amīn 'Alī "al-Raqābah al-Shar'iyah al-Fa'ālah Fī al-Maṣārif al-Islāmiyyah " Paper presented at the TheThird International Conference on Islamic Economics, Mecca, 31/5-2/06/2005.
- Qayum, Khalid , and Soraya Permatasari. "Shariah Experts Push for Certification of Islamic Scholars." Bloomberg <http://www.bloomberg.com/news/2010-08-31/shariah-experts-prepare-first-certification-of-scholars-islamic-finance.html>. accessed 15 October 2010
- QIB(UK). "Our People " QIB Bank(UK) <http://www.qib-uk.com/html/our-people.asp>. accessed 28 August 2011
- "Quran." Oxford University Press, <http://www.oxfordislamicstudies.com/opr/t125/e1945>. accessed 04/12/2010
- Rammal, Hussain Gulzar. "The Importance Of Shari'ah Supervision In Islamic Financial Institutions." *Corporate Ownership and Control Journal* 3, no. 3 (2006): 204-08.
- Rane, Halim. "Issues in Legal Thought." In *Islam and Contemporary Civilisation : Evolving ideas, Transforming Relations*. Melbourne, Vic.: Melbourne University Publishing, 2010
- Rasul, Bilal "Identifying the Main Regulatory Challenges for Islamic Finance." Bloomsbury Publishing, <http://www.qfinance.com/regulation-best-practice/identifying-the-main-regulatory-challenges-for-islamic-finance?full>. accessed 25 June 2012
- Remo-Listana, Karen "Islamic Finance Standardisation Needs to be Tackled Carefully." Dubai Media Inc, <http://www.emirates247.com/eb247/banking-finance/islamic-finance/islamic-finance-standardisation-needs-to-be-tackled-carefully-2009-10-25-1.18970>. accessed 15 June 2012
- Rezaee, Zabihollah. *Corporate Governance and Ethics*. Hoboken, NJ: John Wiley & Sons, 2009.
- Richter, Frederik. "Top Islamic Finance Scholars Oppose Reform Effort." Reuters, <http://www.reuters.com/article/2010/12/01/islamicfinance-scholars-idUSLDE6B015920101201>. accessed 3 December 2010
- Rider, Barry. "Corporate Governance of Institutions Offering Islamic Financial Services." In *Islamic Finance: Law and Practice*, edited by Craig Nethercott and David Eisenberg. Oxford: Oxford University Press, 2012
- Riyad Bank. "Annual Report." Riyad Bank, <http://www.riyadbank.com/PDF/reports/annualreports/en/2010/AnnualReport2010.pdf>. accessed 28 August 2011

- Riyad Bank. "Islamic Banking "
<http://www.riyadbank.com/English/PersonalBanking/IslamicBanking.html>. accessed 28 August 2011
- Rosman, Arieff Salleh "al-Ḥiyal wa al-Makhārij fī al-Mu‘āmalāt al-Maṣrifīyyah al-Islāmiyyah." PhD thesis International Islamic University of Malaysia, 2008.
- SABB. "Annual Report." SABB Bank
http://www.sabb.com/1/PA_1_083Q9FJ08A002FBP5S00000000/content/SABB/en/about_us/attachments/annual_reports/sabb_annual_report_2010_en.pdf. accessed 28 August 2011
- SABB. "Shariah Committee." SABB Bank, http://www.sabb.com/1/2/sabb-en/about-us/profile/sahariah_advisory_commitee. accessed 28 August 2011
- Safieddine, Assem. "Islamic Financial Institutions and Corporate Governance: New Insights for Agency Theory." *Corporate Governance: An International Review* 17, no. 2 (2009): 142–58.
- Saheeh International. *Translation Of The Meanings Of The Glorious Quran*. al-Muntada al-Islami, 2004.
- SAMA. "Implementing Regulations of The Law on Supervision of Finance Companies (Arabic) " SAMA,
[http://www.sama.gov.sa/sites/samaen/Finance/FinanceLib/L_EN_ImplementingRegulationsOfTheLawOnSupervisionOfFinanceCompanies\(Arabic\).pdf](http://www.sama.gov.sa/sites/samaen/Finance/FinanceLib/L_EN_ImplementingRegulationsOfTheLawOnSupervisionOfFinanceCompanies(Arabic).pdf). accessed 10 May 2013
- SAMA. "Laws and Regulations." SAMA,
<http://www.sama.gov.sa/sites/samaen/RulesRegulation/Pages/Home.aspx>. accessed 13 May 2013
- Samad, Syed Abdus, Norman D Gardner, and Bradley J Cook. "Islamic Banking and Finance in Theory and Practice: The Experience of Malaysia and Bahrain." *The American journal of Islamic social sciences*. 22, no. 2 (2005): 69-86.
- SAMBA. "Annual Reports." Samba Bank,
http://www.samba.com/English/Common/HTML/abtSambaFReports_01_01_en.html. accessed 28 August 2011
- SAMBA. "Islamic Products." Samba Bank,
http://www.samba.com/ENGLISH/CONSUMER/HTML/CONSISLAMICPRODUCTS_01_01_en.html. accessed 28 August 2011
- Sano, Koutoub Moustapha. *Mu‘jam Muṣṭalaḥāt Uṣūl al-Fiqh*. Damascus: Dar al-Fikr, 2000.
- Saudi Arabia. "The Basic Law of Governance."
<http://www.mofa.gov.sa/sites/mofaen/aboutKingDom/SaudiGovernment/Pages/BasicSystemOfGovernance35297.aspx>. accessed 11 May 2013
- Saudi Arabia. "Capital Market Law " Capital Market Authority (CMA),
<http://www.cma.org.sa/En/AboutCMA/CMALaw/Documents/CAPITAL%20MARKET%20LAW-26-8-009.pdf>. accessed 25 September 2011
- Saudi Arabia. "Charter of the Saudi Arabian Monetary Agency." SAMA,,
<http://www.sama.gov.sa/sites/samaen/RulesRegulation/BankingSystem/Pages/BankingSystemFD01.aspx>. accessed 12 May 2013
- Saudi Hollandi Bank (SHB). "Shari‘ah Board Members."
<http://shb.com.sa/en/about/AboutSHB/ShariahBoardmembers.aspx>. accessed 28 August 2011
- Saudi Hollandi Bank(SHB). "Annual Report "
http://www.shb.com.sa/PDF/SHB%20Annual%20Report%202010_English.pdf. accessed 28 August 2011
- Schacht, Joseph. "Ahl al-Ḥadīth." In *Encyclopaedia of Islam*: Brill, 2012
 <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/ahl-al-hadith-SIM_0379> accessed 1 April 2012
- Schacht, Joseph. "Ḥiyal." In *Encyclopaedia of Islam*: Brill 2012
 <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/hiyal-SIM_2913> accessed 1 April 2012

- Schacht, Joseph. *An Introduction to Islamic Law*. Oxford: Oxford University Press, 1982.
- Sechafia, Nus, Saim Kayadibi, Ibrahim Guran Yumusak, and Hamza Ates. "What Drives An Ideal Islamic Finance? A Maqasid Compliance Approach." Paper presented at the International Business and Social Sciences and Research Conference, Cancun, Mexico,, 16 - 17 /12/ 2013.
- Securities Commission. "Members Of The Sc's Shariah Advisory Council." SC,, <http://www.sc.com.my/main.asp?pageid=251&menuid=277&newsid=&linkid=&type> . accessed 15 May 2013
- Shamil Bank Bahrain v. Beximo Pharmaceuticals Limited & Ors [2003] EWHC 2118*, (2003).
- Shandī, Ismā'īl, and Taqīal-Dan 'abd al-bāsiṭ. "al-Qirā'āt al-Qur'āniyyih wa Atharuhā fī Akhtil-āaf al-Fuqahā'." *Majallah Jāmi'ah al-Quds al-Maftūhah lil-'bḥāth wa al-Dirāsāt*, no. 8 (2006): 307.
- Shariyah Review Bureau. "About Us." Shariyah Review Bureau,, http://www.shariyah.com/?page_id=15. accessed 18 May 2013
- Shinsuke, Nagaoka "Beyond the Theoretical Dichotomy in Islamic Finance: Analytical Reflections on Murābahah Contracts and Islamic Debt Securities." *Kyoto Bulletin of Islamic Area Studies on Islamic Finance* 1, no. 2 (2007): 72.
- Shoeb, Mohammad. "Present Islamic banks no different from other banks, experts lament." *Peninsula Newspaper*.
- Shura Sharia Consultancy. "Home." Shura,, <http://www.shura.com.kw/home/pages/default.aspx>. accessed 18 May 2013
- Siddiq, Mohammad Nejatullah. "Economics Of Tawarruq: How Its Mafasid Overwhelm The Masalih." http://www.siddiqi.com/mns/Economics_of_Tawarruq.pdf. accessed 8 August 2011
- Siddiq, Mohammad Nejatullah. "The Wisdom of Prohibition of Interest." www.siddiqi.com, http://www.siddiqi.com/mns/Interest_Prohibition.html. accessed 1 March 2014
- Siddiqi, Mohammed Nejatullah. "Banking and Finance in Theory and Practice: A Survey of the State of the Art." *Islamic Economic Studies* 13, no. 2 (2006): 1-48.
- Siddiqi, Muhammad Zubair. *Hadith Literature : Its Origin, Development and Special Features*. Cambridge: Islamic Texts Society, 1993.
- Siddiqui, Rushdi. "A Sharia Scholar's Place on The Board." Gulf News, <http://gulfnews.com/business/features/a-sharia-scholar-s-place-on-the-board-1.625445>. accessed 30 October 2010
- Simply Sharia. "About " Simply Sharia,, <http://www.simplysharia.com/About/1/>. accessed 14 May 2013
- Singh, Habhajan. "BNM mulls 5 Shariah Advisors for Islamic Banks." *Malaysian Reserve* 25 October 2010.
- Singhal, Ashish Kumar, and Ikramuddin Malik. "Doctrinal and socio-legal methods of research: merits and demerits." *Educational Research Journal* 2, no. 7 (2012): 252-56.
- Sole, Juan. "Introducing Islamic Banks into Coventional Banking Systems." (2007) *IMF Working Paper No. 07/175* (2007): 1-24. <http://ssrn.com/abstract=1007924> accessed 12 September 2011
- State Bank of Pakistan. "Instructions for Shariah Compliance In Islamic Banking Institutions." State Bank of Pakistan <http://www.sbp.org.pk/ibd/2008/Annex-c2-1.pdf>. accessed 25 January
- Stevenson, Angus. "Oxford Dictionary of English." Oxford University Press, http://www.oxfordreference.com/views/BOOK_SEARCH.html?book=t140. accessed 1 November 2011
- Strohm, Christiane. *United States and European Union Auditor Independence Regulation: Implications for Regulators and Auditing Practice*. Wiesbaden: Deutscher Universitäts-Verlag, 2006.
- Sudan. "The Banking Business Organisation Act (2003)." CBOS,, <http://www.cbos.gov.sd/en/node/434>. accessed 27 May 2013

- Summer, Martin. "Does Mandatory Rotation Enhance Auditor Independence." *Zeitschrift für Wirtschafts- und Sozialwissenschaften* 118, no. 3 (1998): 327.
- Swain, Harriet. "Islamic Finance Gives Universities a Bonus." *The Guardian*, 28 July 2009, 7.
- Taylor, John B. . "Understanding and Supporting Islamic Finance: Product Differentiation and International Standards." Paper presented at the Islamic Finance: Current Legal and Regulatory Issues, Cambridge, 8 /5/ 2004.
- The Association for Islamic Finance Advancement (AIFA). AIFA,, <http://aifa-i.org/>. accessed 30 May 2011
- The Auditing Practices Board. "APB Ethical Standard 5: Non-Audit Services Provided To Audited Entities " Financial Reporting Council (FRC),, [https://www.frc.org.uk/Our-Work/Publications/APB/ES-5-\(Revised\)-Non-audit-services-provided-to-\(2\).pdf](https://www.frc.org.uk/Our-Work/Publications/APB/ES-5-(Revised)-Non-audit-services-provided-to-(2).pdf). accessed 1 March 2014
- The General Council for Islamic Banks And Financial Institution (CIBAFI). "About CIBAFI." CIBAFI,, <http://www.cibafi.org/Pages.aspx?id=pvRm8sofDxI=>. accessed 16 May 2013
- The Higher Sharia Supervisory Board for Banks & Financial institutions (HSSB). *Nash'at Wata'awwur Wataqwim Ha'at al-Riqābah al-Shar'iyyah fī al-Jihāz al-Mašrifī al-Sūdānī* 1ed. Khartoum: Central Bank of Sudan, 2006.
- The International Centre for Education in Islamic Finance (INCEIF). INCEIF,, <http://www.inceif.org/home/papers>. accessed 30 May 2011
- The Islamic Finance Council UK (IFC). IFC,, <http://www.islamicfinancecounciluk.com/>. accessed 23 May 2011
- The Muslim Council of Britain. "Islamic Finance Transparency Standard : a Consultation." MCB,, <http://www.mcb.org.uk/uploads/MCBIslamicFinanceTransparencyStandard.pdf>. accessed 9 May 2013
- The National Commercial Bank. "Annual Report " http://www.alahli.com/en-US/About%20Us/News_Reports/Documents/Reports%202010/NCB%20AR10%20English.pdf. accessed 28 August 2011
- The National Commercial Bank. "The NCB Shariah Board " <http://www.alahli.com/ar-SA/About%20Us/ibd/Pages/TheNCBShariahBoard.aspx>. accessed 28 August 2011
- The Saudi Investment Bank (SAIB). "Financial Statements." <http://www.saib.com.sa/Docs/Financial%20Statements%202010%20English.pdf>. accessed 28 August 2011
- The Saudi Investment Bank (SAIB). "Islamic Banking." <http://www.saib.com.sa/english/islamic.aspx>. accessed 28 August 2011
- The Supreme Constitutional Court of Egypt , Case No. 13 of year 15 6408 (1994).*
- Trumbull, Charles P. "Islamic Arbitration: A New Path for Interpreting Islamic Legal Contracts." *Vanderbilt Law Review* 59, no. 2 (2006): 609-47.
- Turkey. *The Mejelle: Being an English Translation of Majallah El-Ahkam-i-Adliya and a Complete Code on Islamic Civil Law*. Translated by Charles Robert Tyser, D. G. Demtriades and Ismail Haqqi Effendi. Islamic Book Trust, 2001.
- Turki, Abdel-Magid. "al-Zāhiriyya." In *Encyclopaedia of Islam*, edited by P. Bearman, Th. Bianquis, C.E. Bosworth, E. van Donzel and W.P. Heinrichs: Brill Online, 2012 <http://referenceworks.brillonline.com/entries/encyclopaedia-of-islam-2/al-zahiriyya-SIM_8086> accessed 30 April 2012
- U. K. Trade Investment. *The City: UK excellence in Islamic Finance*
London: UK Trade & Investment,, 2008.
- ‘Umar, Muḥammad ‘Abd al-Ḥalīm "A' māl al-Hay'āt al-Shar'īyyah Bayn al-Iāstishāriyyah al-Fardiyyah Wa al-Mihniyyah al-Mu'assasiyyah " Paper presented at the The Third Conference of Shari'a Supervisory Boards of Islamic Financial Institutions, Bahrain, 7-8/10/2003.
- Ünal , Murat "The Small World of Islamic Finance; Shariah Scholars and Governance - A Network Analytic Perspective." Funds@Work, <http://www.funds-at->

- [work.com/fileadmin/downloads/Sharia-Network by Funds at Work AG.pdf.pdf](http://work.com/fileadmin/downloads/Sharia-Network%20by%20Funds%20at%20Work%20AG.pdf.pdf). accessed 5 February 2011
- United Arab Emirates. "Federal Law No-(6) of 1985 concerning Islamic Banks and Financial Institutions and Investment Companies." Central Bank of United Arab Emirates,, <http://www.centralbank.ae/pdf/LawNo6-1985-IslaminBanks.pdf>. accessed 10 November 2011
- United Kingdom. "Company Directors Disqualification Act 1986." The National Archives, http://www.legislation.gov.uk/ukpga/1986/46/pdfs/ukpga_19860046_en.pdf. accessed 10 May 2013
- United Kingdom. "The Consumer Protection from Unfair Trading Regulations 2008." The National Archives, http://www.legislation.gov.uk/uksi/2008/1277/pdfs/uksi_20081277_en.pdf. accessed 16 May 2013
- United Kingdom. "Financial Services Act 2012." The National Archives, http://www.legislation.gov.uk/ukpga/2012/21/pdfs/ukpga_20120021_en.pdf. accessed 17 May 2013
- United Kingdom. "Financial Services and Markets Act 2000 : Chapter 8." The National Archives, http://www.legislation.gov.uk/ukpga/2000/8/pdfs/ukpga_20000008_en.pdf. accessed 15 May 2013
- United Kingdom. "Fraud Act 2006 Chapter 35." The National Archives, http://www.legislation.gov.uk/ukpga/2006/35/pdfs/ukpga_20060035_en.pdf. accessed 10 May 2013
- United National Bank. "Islamic Products." <http://www.unbankltd.com/islamic-products/>. accessed 28 August 2011
- Usman, Mian. "The Islamic Concept of Leadership." Allvoices, Inc, <http://www.allvoices.com/contributed-news/4804200-the-islamic-concept-of-leadership>. accessed 9 August 2011
- Usmani, Muhammad Taqi. *An Introduction to Islamic Finance*. The Hague: Kluwer Law International, 2002.
- Usmani, Muhammad Taqi. "Verdicts on At-Tawarruq and Its Banking Applications." Paper presented at the The 17th session of the International Islamic Fiqh Academy, Makkah, 13- 17/12/ 2003.
- Uthaymin, Muhammad Salih. *Differences of Opinion Amongst The Scholars: Their Causes and our Position Towards Them*. Translated by Abu Safwan Farid Haibatani. Birmingham, U.K.: al-Hidaayah Pub. and Distribution, 1997.
- Vejzagic, Mirza, and Edib Smolo. "Maqasid Al-Shari'ah in Islamic Finance: An Overview." Paper presented at the The 4th Islamic Economic System Conference 2011 (IECONS 2011), Kuala Lumpur, Malaysia, 4-5 /10/ 2011.
- Verhoef, Bastiaan, Somia Azahaf , and Bijkerk Werner. *Islamic Finance and Supervision: an Exploratory Analysis*. Amsterdam: De Nederlandsche Bank, Eurosysteem, 2008.
- Vesey-Fitzgerald, S.G. . "Nature and Sources of the Sharī'a." In *Law in the Middle East*, edited by Majid Khadduri and Herbert J. Liebesny. Washington: The Middle East Institute, 1955
- Vizcaino, Bernardo. "Islamic Scholars Launch Global Professional Association." Reuters <http://www.reuters.com/article/2013/10/30/islamic-finance-idUSL5N0IK3GG20131030>. accessed 2 March 2014
- Vizcaino, Bernardo. "Oman plans Islamic finance rules before year-end." Reuters, <http://in.reuters.com/article/2012/06/27/islamic-finance-regulation-idINL6E8EU1VI20120627>. accessed 10 March 2013
- Vogel, Frank E., and Samuel L. Hayes. *Islamic Law and Finance: Religion, Risk, and Return*. The Hague: Kluwer Law Internat., 1998.
- Warde, Ibrahim. *Islamic Finance in The Global Economy*. Edinburgh: Edinburgh University Press, 2000.
- Weiss, Bernard. "Interpretation in Islamic Law: The Theory of Ijtihad." *The American Journal of Comparative Law* 26, no. 2 (1978): 199.

- Weiss, Bernard. *The Spirit of Islamic Law*. Athens, University of Georgia Press, 1998.
- Wigglesworth, Robin "Sharia Boards: Scholars Hold Sway over The Success of Products." *The Financial Times*, <http://www.ft.com/cms/s/0/91c1636e-3836-11de-9211-00144feabdc0.html#axzz1y8yjhBuO>. accessed 18 June 2012
- Wilson, Rodney. "The Development of Islamic Finance in the GCC." *LSE Centre for the Study of Global Governance, May 2009* (2009).
<http://www2.lse.ac.uk/government/research/resgroups/kuwait/documents/Wilson.pdf>
accessed 10 November 2010
- Wilson, Rodney. *Islamic Finance in Europe*. Florence: European University Institute, 2007.
- Wilson, Rodney. "Regulatory Challenges Posed by Islamic Capital Market Products and Services." *Journal of Islamic Banking and Finance* 24[2], no. 2 (2007): 18-36.
- Wright, Chris. "The Shariah Scholar Cartel." *Asiamoney*,
<http://www.chriswrightmedia.com/asiamoney-sep06-shariahscholars/>. accessed 20 April 2011
- Yaacob, Hakimah. "A Critical Appraisal of International Islamic Finance Cases and the Way Forward." *ISRA Research Paper No. 19/2011* (2011). <http://www.isra.my/media-centre/downloads/view.download/29-isra-research-paper/293-a-critical-appraisal-of-international-islamic-finance-cases-and-the-way-forward-no-192011.html> accessed 30 October 2012
- Yaacob, Hakimah. "The New Central Bank Of Malaysia Act 2009 (Act 701): Enhancing The Integrity And Role of The Shariah Advisory Council (SAC) in Islamic Finance." *ISRA Research paper 6/2010*. (2010).
<http://www.kantakji.com/fiqh/Files/Markets/B103.pdf> accessed 10 May 2013
- Yaacob, Hakimah, Marjan Muhammad, and Edib Smolo. "International Convention For Islamic Finance: Towards Standardisation ", *ISRA Research Paper (No. 29/2011)* (2011). <http://www.isra.my/publications/research-paper/research-paper/item/858-research-paper-no-29/2011.html> accessed 20 June 2012
- Yemen. " Act 21(1996) as amended by Act 16 (2009) on Islamic Banks in Yemen." Central Bank of Yemen,,
http://www.centralbank.gov.ye/App_upload/Islamic_Pank_low_Ar_Upd.pdf.
accessed 8 July 2011
- Yerushalmi, D. "Shari'ah's ``Black Box": Civil Liability and Criminal Exposure Surrounding Shari'ah-Compliant Finance." *Utah law review.*, no. 3 (2008): 1019-106.
- Yeung, Karen. *Securing Compliance : a Principled Approach*. Oxford: Hart Pub, 2004.
- Zāhīr, 'Uthmān. "Bay' al-Maḥāwīj." *al-Āqtiṣādiyyah*, 2 September 2007.
- Zahraa, Mahdi. "Unique Islamic Law Methodology and the Validity of Modern Legal and Social Science Research Methods for Islamic Research." *Arab law quarterly Arab law quarterly* 18, no. 3-4 (2003): 215-49.
- Zaidi, Jamal Abbas "Shari'a Harmonization, Regulation and Supervision." Paper presented at the AAOIFI-World Bank Islamic Banking and Finance Conference, Manama, 10/11/2008.
- Zaman, Arshad, and Asad Zaman. "Interest and the Modern Economy." *Islamic Economic Studies* 8, no. 2 (2001): 61.
- Zighībah , 'Izz al-Dīn "Hay'āt al-Fatwā Wa al-Riqābah al-Shar'īyyah Fī al-Mu'asasāt al-Māliyyah al-Islāmiyyah Ahammiyyathā Mu'awwiqāt 'Amalhā wa Ḥulūl Muqtarahah " Paper presented at the Islamic Banking Between Reality and Expectations, Dubai, UAE, 31 /5/ 2009