Article

Encounters between legal systems: recent cases concerning Islamic commercial law in secular courts

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The revival of interest in Islamic law prompts a number of questions, including its suitability for the modern commercial world, and the appropriateness of western-style courts for enforcement of the sharia.

INTRODUCTION

In recent years there has been a revival of interest in Islamic law or, to be more accurate, the two distinct, but overlapping, concepts of *sharia* and *fiqh*. The *sharia* (stress on the second syllable, to rhyme with "Korea" rather than with "carrier") has a much wider ambit than the Western concept of "law". It governs "the Muslim's way of life in literally every detail, from political government to the sale of real property, from hunting to the etiquette of dining, from sexual relations to worship and prayer" (Hallaq, W B (2003) "'Muslim Rage' and Islamic Law" (54) *Hastings Law Journal* 1705, p 1707). The literal meaning of *fiqh* is "understanding." It is often translated as "Islamic jurisprudence", and has been described as "the scholarship of rule-making" (Khalafallah, H (2001) "The Elusive 'Islamic Law': Rethinking the Focus of Modern Scholarship" (12) *Islam and Christian Muslim Relations* 143, p 144). Manifestations of the revival include the development of Islamic finance and the enactment of "Islamic" statutes in Muslim-majority jurisdictions.

This article considers an intriguing consequence of the revival, the encounter of the sharia with Western-style legal systems in some recent cases.

THE ENCOUNTERS

Contemporary legal systems, whether in Muslim-majority jurisdictions or in the West, are nearly all state-based for, as a result of "modernisation", most Islamic legal systems of the classical era were dismantled and replaced by European regimes (Hallaq, "'Muslim Rage'" pp 1711–14). This is true even of Gulf states, the regimes of which are based, to a greater or lesser degree, on the sharia. So whether one attempts to follow the principles of the sharia in one's financial dealings within a Western law context, or one attempts to incorporate rules based on the sharia into a state-based legal system, Western and Islamic legal mindsets come into contact.

In the last few years we have seen intriguing examples of such encounters in the courts of the United Arab Emirates (the UAE), Malaysia and England.

England: Symphony Gems and Beximco

In England, two Islamic finance cases have come before the courts. One was heard before the High Court (*Islamic Investment Company of the Gulf (Bahamas) Ltd v Symphony Gems NV & Ors* unreported 2002 WL 346969, [2002] All ER (D) 171 (Feb) (QBD: Comm Ct), available on LexisNexis, comment in Bälz, K (2004) "A Murabaha Transaction in an English Court: The London High Court of February 13, 2002 in *Islamic Investment Company of the Gulf (Bahamas) Ltd v Symphony Gems NV & Ors*' (11) *Islamic Law and Society* 117: the *Symphony Gems* case); the other (*Shamil Bank of Bahrain EC v Beximco Pharmaceuticals Ltd* [2004] EWCA Civ 19; [2004] 1 WLR 1784 (CA), at first instance [2003] EWHC 2118; [2003] 2 All ER (Comm) 849, comment in Bälz, K (2005) "Islamic Financing Transactions in European Courts" in Ali, SN (ed) *Islamic Finance: Current Legal and Regulatory Issues* Islamic Finance Project, Islamic Legal Studies Program, Harvard Law School, particularly at 65-67: the *Beximco* case), reached the Court of Appeal.

Islamic finance transactions are designed to avoid *riba*. *Riba* can be roughly described as unlawful gain. It is clearly forbidden by the Koran, but there is no universally agreed definition. Most jurists agree that interest constitutes *riba*, but the popular belief that interest and *riba* are the same is wrong, because the ambit of *riba* is considerably wider than that of interest. Sale, however, is permitted. In this connection, a well known verse of the Koran (II: 275) is often quoted:

قالوا إنما البيع مثل الربا وأحل الله البيع وحرم الربا

They said that sale is like riba *whereas Allah has allowed sale and has banned* riba.

Both cases concerned a commonly used type of contract, the *murabaha*. Rather than a bank lending money at interest to a client wishing to purchase goods in return for the grant of a security interest on those goods, the bank buys the goods itself, then sells them to the client at a higher price agreed in advance. For this reason it is also called the "cost-plus-profit" contract. Unsurprisingly, the difference in price is the same amount as the client would have paid in the conventional, *riba*-based loan transaction. In both cases the documents were governed by English law. They differed, though, in the way in which the drafters attempted to subject the transactions to the sharia.

In *Symphony Gems* the attempt was contained in a mere recital, to the effect that: "The Purchaser wishes to deal with the Seller for the purpose of purchasing Supplies [...] under this Agreement in accordance with the Islamic Shari'ah." Presumably as a result of the negligible effect usually given to recitals, Tomlinson J felt able to brush the reference to the sharia aside, saying: "it is a contract governed by English law. I must simply construe it according to its terms as an English law contract."

In *Beximco*, however, the reference to the sharia was contained in the governing law clause and was therefore the subject of considerable discussion. It read: "Subject to the principles of the Glorious Shari'a, this Agreement shall be governed by and construed in accordance with the laws of England." Morison J found at first instance that Article 1.1 Rome Convention (Convention on the Law Applicable to Contractual Obligations, Rome 1980), enacted into English law by section 2(1) Contracts (Applicable Law) Act, 1990, could not be construed so as to permit the sharia to be the applicable law of a contract, as it is not the law of a "country" (paras 27 and 35). Reference was also made to Article 3.1 ("the law chosen by the parties", rather flimsy support in this author's view) and Article 3.3 (much stronger support, containing references to "foreign law" and "country"). This finding was not contested on appeal (paras 43 and 48).

Also, counsel for the appellant conceded at first instance that it was impossible for two systems of law to govern the contract (paras 28–30 of Morison J's judgment, referring to *American Motor Insurance Co v Cellstar Corpn* [2003] EWCA Civ 206, [2003] All ER (D) 26 (Mar) at 32). He contended, though, that the parties had stipulated "as a condition precedent that the contract is only to be enforceable insofar as it is consistent with the principles of Shari'a, which principles amount to legal rules ascertainable and applicable by an English Court" (para 42). In other words he claimed that the sharia was incorporated by reference, something allowed by English law (para 43, referring to *Nea Agrex SA v Baltic Shipping Co Ltd* [1976] 1 QB 933 (CA)), and that the incorporation was specific enough to be meaningful, because it incorporated "simply those specific rules of Shari'a which relate to interest and to the nature of Morabaha and Ijarah contracts, thus qualifying the choice of English law as the governing law only to that extent" (para 49, summarising the appellant's argument).

However, Potter LJ (who gave the judgment of the court, Laws and Arden LJJ concurring) based his reasoning squarely on contractual interpretation, saying: "The central question in this appeal is one of construction" (para 46). The English approach to interpretation is, of course, "to ascertain the presumed intention of the parties" in the context of "the commercial purpose of the contract[,] the genesis of the transaction, the background, the context [and] the market in which the parties are operating" (id, referring to Lord Wilberforce's speech in *Reardon Smith Line Ltd v Yngvar Hansen-Tangen* [1976] 1 WLR 989 at 996). He reasoned that, since all the parties knew perfectly well that the arrangements really amounted to loans, and they always intended to be bound by the terms of the contracts, the governing law clause should be construed so as to give effect to the commercial purpose of the contracts, in other words, so as to give effect to them as loans.

As for the appellant's argument on incorporation he held, in effect, that only a clear reference to "sufficiently identified specific 'black letter' provisions [...] such as a particular article or articles of the French Civil Code or the Hague Rules" (para 51) could displace the initial conclusion he had reached, and that the reference to the sharia was too vague to achieve this result. "The general reference to principles of Shari'a in this case affords no reference to, or identification of, those aspects of Shari'a law which are intended to be incorporated into the contract, let alone the terms in which they are framed" (para 52). Being merely "a reference to the body of Shari'a law generally", it made the clause "self-contradictory and therefore meaningless" (ibid), presumably meaning that this interpretation resulted in the agreements being governed by two "contradictory" laws, English law and the sharia, a result which, as seen above, is in any event not permitted. This was because "the words are intended simply to reflect the Islamic religious principles according to which the Bank holds itself out as doing business rather than a system of law intended to 'trump' the application of English law as the law to be applied in ascertaining the

liability of the parties under the terms of the agreement" (ibid).

The decision has been welcomed by the banking community and their lawyers, for it tells us that the English courts will enforce Islamic finance documents governed by English law in accordance with their terms.

Malaysia: The Affin Bank *case*

In *Affin Bank Berhad v Zulkifli Abdullah* ([2006] 1 *Current Law Journal* 438, Bernama, December 29, 2005, summary at http://www.malaysianbar.org.my/content/view/2174/2/ (last visited July 15, 2006): the case is to be the subject of a study by Dr Ahmad Hidayat Buang), the Commercial Division of the Kuala Lumpur High Court had to deal with an "Islamic mortgage" of the form called "Al-Bai Bithaman Ajil". In this transaction, the bank buys the property, then sells it to its customer at a higher price on deferred payment terms. The aim is to avoid the *riba* associated with a "conventional" loan against the security of a mortgage. The difference between the price paid by the bank and the price paid by its customer is equivalent to the amount of interest which would have been payable in a conventional mortgage arrangement. In this case the purchaser/borrower was an employee of the bank at the time of the transaction. He left the employ of the bank shortly afterwards. Some time later he defaulted on the payments. The sum of the original price paid for the house and unpaid instalments to the date of the claim was RM582,000 (c£84,000: RM = Malaysian Ringgit or Malaysian Dollar; all conversions made on July 15, 2006). The bank, however, sued for the original price plus all sums payable by the purchaser/borrower over the 18 year term of the agreement, a total of almost RM959,000 (c £138,000). The market value of the house was estimated to be of the order of RM400,000 (c £57,600). Abdul Wahab Patail J greeted the bank's claim with a degree of consternation.

> *When the gratification of being able to satisfy the pious desire to avoid financing containing the elements of Riba gives way to the sorrow of default before the end of tenure of an Al-Bai Bithaman Ajil facility, the revelation that even after the security had been auctioned at full market value there remains still a very substantial sum owing to the bank, comes as a startling surprise. All the more shocking when it is further realised that a borrower under a Riba-ridden loan is far better off ([2006] 1* Current Law Journal *at 446).*

A preliminary issue was whether a reference should be made to the National Syariah [sharia] Advisory Council, a body which verifies the Islamic credentials of all new banking products bearing an "Islamic" label. Understandably, since the SAC is not a court the judge, guided by a decision of the Court of Appeal (*Bank Kerjasama Rakyat Malaysia v Emcee Corporation* [2003] 1 *Current Law Journal* 625, per Abdul Hamid Mohamed JCA), came to the conclusion that this should not be done, because "reference of this case to another forum for a decision would be an indefensible abdication by this court of its function and duty to apply established principles to the question before it. It is not a question of Syariah [sharia] law" ([2006] 1 *Current Law Journal* at 448). He then examined the relatively sparse previous case-law, and decided that previous decisions had not considered the main point, whether "the provider of an Al-Bai Bithaman Ajil facility is entitled to the profit margin for the whole original tenure when the facility is terminated before the end of its tenure" ([2006] 1 *Current Law Journal* at 448), and he was therefore not bound by precedent in this matter.

In a chain of reasoning which is intriguing to compare with that of the English Court of Appeal in *Beximco,* Patail J, following the approach of the Supreme Court in *Malayan Banking Bhd v PK Ralamani* ([1994] 2 *Current Law Journal* 25 (SC), cited at [2006] 1 *Current Law Journal* 448), looked beyond the words in the document to the substance of the transaction and to its economic effect and justification. Perhaps with the common law principle of the equity of redemption consciously or unconsciously in his mind (ie a grantor of security is entitled to the balance remaining from realisation of the secured asset after satisfaction of the debt), he pointed out that the bank's profit was not to be made by means of the simple difference between the purchase price and the sale price, but arose from the long-term nature of the transaction, being "a function of the bank purchase price, the agreed profit rate [...] and the agreed tenure of the facility [and] paid by monthly instalments according to the number of months in the tenure of the facility."

In other words, the customer and the bank had agreed that the customer would enjoy the benefit of the arrangement for the duration of the facility and would pay the bank its profit for that period. So "it would be inconsistent with his right to the full tenure if he could be denied the tenure and yet be required to pay the bank's profit margin for the full tenure" (id at 450). In addition, the bank would be able to make a profit on sums recovered from the customer for the remainder of the tenure, earning profit twice on the same money. Somewhat curiously, given that the High Court is a secular forum, and his statement that the issue was "not a matter of Syariah [sharia] law" (id at 448), he claimed that the fact that this would be unearned profit "contradicts the principle of Al-Bai Bithaman Ajil as to the profit margin that the provider is entitled to". He also said that: "if the profit has not been earned it is not profit, and cannot be claimed under the [...] facility" (ibid).

The judge therefore reduced the amount of the claim to RM582,000, the price plus unpaid instalments.

The UAE: assignments in the Federal Supreme Court

In 2001 the UAE Federal Supreme Court in Abu Dhabi, although normally regarded as more conservative than its counterpart in Dubai (the UAE is a federal state but Dubai has its own court system, supervised by a separate Supreme Court), sanctioned as legally valid a Western (French) style transfer of rights with notice to, rather the consent of, the debtor. (Federal Supreme Court No 693/21 (2001), English text and comment in Al Ulama, AW (2002) "Supreme Court Judgment No 693 for the Year 21 Delivered on 18/11/2001" (139) *Law Update* 12, available at http://www.tamimi.com/catalog/1998_2004/issue139October2002.pdf (last visited July 11, 2006); further comment in Foster, NHD (2004) "An Unstoppable Force Meets a Movable Object? Assignment of Rights in the UAE", (19) *Arab Law Quarterly* 169.)

The situation regarding transfers of rights in the sharia is complex, but very briefly Western-style transfers were not generally permitted, and although it is difficult to tell for certain, it seems that the drafters of the UAE Civil Code (Civil Transactions Law of the United Arab Emirates, enacted by Federal Law No 5 of 1985, as amended by Law No 1 of 1987), unlike their counterparts in Egypt and Kuwait, intentionally omitted to include a provision allowing them. All they inserted was an equivalent to the sharia rules providing for the transfer of rights in very limited circumstances (Arts 1106ff).

The most likely explanation of the ruling, in which clear provisions regarding the Islamic nature of UAE law and legal reasoning, such as Article 1 Civil Code (recourse to the sharia in the case of a lacuna), Article 2 (interpretation), Article 3 (public policy) and Article 96 (certainty), were ignored, seems to be the European mindset of the judges. But one must add that the obscure nature of the part of the sharia concerned did not provide a serious obstacle to that mindset.

SOME QUESTIONS AND SOME ATTEMPTS AT ANSWERS

To sum up. One court in a Muslim-majority jurisdiction has sanctioned the introduction of a Western-style transfer of rights, probably as a result of the Western mindset of the judges. Another court in a Muslim-majority jurisdiction has refused to give effect to an Islamic transaction because, in the opinion of a judge who might well have been influenced by the common law idea of the equity of redemption, it produced an unjust result. Two courts in a Western jurisdiction have refused to give effect to words purporting to make contracts subject to sharia principles.

At least two questions come to mind.

Suitability for the modern commercial world

First question: is the sharia unsuitable for the modern commercial world?

Take the alleged "controversy and difficulty arising [...] from the need to translate into propositions of modern law texts which centuries ago were set out as religious and moral codes" (para 55 of Potter LJ's judgment in *Beximco*). In other words, the sharia is religion, not law. With the greatest respect to the Court of Appeal, this is a misreading of the situation. Although, as seen above, the sharia is certainly tied to religion in a way which is quite different from Western regimes, and covers all sorts of areas which Western law does not, the "translation into propositions of law" was done by the jurists many centuries ago. The rules of *mu'amalat* (relating to criminal, family and commercial matters), although religiously inspired, were clearly and recognisably legal in the Western meaning of that word. Despite some uncertainty and academic controversy, thanks to such studies as that of Professor Nelly Hanna on the legal records relating to the daily use of the law and the courts by a successful merchant, we know that the sharia did, on the whole, provide very practical, workable rules (Hanna, N (1998) *Making Big Money in 1600: The Life and Times of Isma'il Abu Taqiyya, Egyptian Merchant* Syracuse University Press, p 59 and passim).

The adaptation to modern conditions is another matter. It must be acknowledged that the process presents difficulties. One is that the sharia rules were designed for a very different economic and technological environment. Another is that there is no agreed method for determining the content of the law, a difficulty which is exacerbated by the modern wish to create uniformity, in contrast to the diversity of legal thought of the past contained in the legal schools and the internal variation of opinion within them. The *Affin Bank* case highlights the further problem that, in at least one instance, an adaptation of a mechanism from the classical era has turned out to be unjust in certain circumstances. Finally, the UAE assignment case seems to show that, in at least one instance, the sharia is out of step with "modern" (ie Western) conceptions.

As regards adaptation, much progress has been and continues to be made in devising products which are generally if not universally regarded as Islamic and which function well in contemporary markets.

Regarding uncertainty, it is true that it is greater than that experienced in a secular, state-based regime such as English law. The mechanisms of the classical period, which might have been used for adapting the sharia to modern life, are no more, whereas English law has a legislature and a system of courts, one of the functions of which is to develop, and maintain a degree of certainty in, the content of the law. However, the difficulties are not insuperable here either. As in other fields, there is in Islamic finance "a process of reconstruction of *shari'a*" (Arabi, O (2001) *Studies in Modern Islamic Law and Jurisprudence,* Kluwer Law International, p 200), based on the deduction of principles from the literature of various schools, which is resulting inter alia in an increase in certainty. Various projects (which are still admittedly in their early stages) have been

undertaken, including the setting up of the Islamic Financial Services Board (standardisation of products), the International Islamic Rating Agency (assessment and grading of the management of agencies), the Accounting and Auditing Organisation for Islamic Financial Institutions (production of numerous standards on accounting and auditing, governance and sharia observance) and the International Islamic Financial Market (includes standardisation and consistency).

Longer-standing institutions include the Institute of Islamic Research (*Majma' Al-Buhuth Al-Islamiyyah* of Al-Azhar University in Cairo (set up in 1961), the Islamic Jurisprudence Institute (*Al-Majma' Al-Fiqhi Al-Islami*) of the Islamic League (*Rabita Al-'Alam Al-Islami*) (set up in 1979), the Fiqh Institute or Academy (Majma' Al-Fiqh Al-Islami) of the Organization of Islamic Conference (OIC: *Munazammat Al-Mu'tamar Al-Islami*), operating in Jedda, Saudi Arabia (set up in 1984); according to Professor El-Gamal, the last mentioned "is currently the most widely cited jurisprudential council, which is comprised of representatives from Islamic members of the OIC" (El-Gamal, MA (2003) " 'Interest' and the Paradox of Contemporary Islamic Law and Finance", (27) *Fordham International Law Journal* 108, 114; the list in this sentence comes from pp 113–114 of Professor El-Gamal's article).

In addition, the number of Islamic scholars is small, resulting in a high level of uniformity; there is a significant amount of standardised best practice; and the documents are more standardised than in the past. One author does argue that, since each financial institution regards its products as valuable property the details of which it tries to keep secret, there is "little standardization and information sharing" (Smith, K (2005) "Islamic Banking and the Politics of International Financial Harmonization" in Ali SN (ed) *Islamic Finance: Current Legal and Regulatory Issues* Islamic Finance Project, Harvard Law School, p 185). However, such secrecy cannot be sustained for ever, as the law firms which draft the documents own the copyright in them and cannot be prevented from using them for other clients, and knowledge of the documents will inevitably circulate to some extent.

The overall result, according to a leading practitioner, is that Islamic finance scholars agree on the vast majority of issues. Problems are, naturally, still identified, but deals no longer collapse in the way they once did (Neil Miller of Norton Rose in a conversation on May 2, 2006).

On the question of the unfairness produced by the documentation in the *Affin Bank* case, the "Islamic" mechanism concerned would indeed have produced a result which seems unjust had the court not intervened. However, this does not prove that the sharia cannot be adapted to the modern world, just that this particular transaction type needs amending. It is hardly fatal to Islamic finance that a problem arises which needs resolution in order to ensure that a mechanism produces a fair result as well as being formally in compliance with the rules devised by the jurists of many centuries ago. All legal systems face similar problems. Mechanisms are devised; unexpected, and sometimes unfair, consequences result. All this means is that the law needs adjustment. In a similar context, English law only managed to devise the equity of redemption and the doctrine of undue influence several centuries after the invention of the mortgage. One might go further and point out that approval of a mechanism in the context of Islamic finance does not necessarily mean that that mechanism is absolutely and completely Islamic, although the author stresses that, as a non-Muslim, he is not qualified to hold an opinion on the Islamicity of a transaction type.

The situation which was evidenced by the UAE assignments case may be the only one which constitutes a truly unsquarable circle. It does seem on the surface that the sharia rule runs counter to the modern trend, that "each society in which commerce plays a role sooner or later has to face a strong demand to increase the circulation of credit" (Zimmermann, R (1990) *The Law of Obligations: Roman Foundations of the Civilian Tradition* Kluwer Law International, p 59). Even here, though, other considerations must be taken into account. For example, the schools differed markedly in this area, so that one can justifiably say that *hawala* (the sharia term for transfers of rights/obligations, often translated as "assignment", although such a translation is highly misleading) is no more than a name for various mechanisms which developed so differently that all they share is the name and their roots in the idea of transfer. (On the variations, see Ray, N D (1997) "The Medieval Islamic System of Credit and Banking: Legal and Historical Considerations", (12) *Arab Law Quarterly* 43, pp 60–65.) One also needs to bear in mind that custom (*'urf*) and legal stratagems (*hiyal*) played a prominent part in commercial law in the classical age, so the impression given by a study of basic principle is deceptive. We know that in Hanafi law, for example, the ban was circumvented (id pp 61–62). The conclusion may therefore be that there was no "sharia rule" in this area, that in the reformulation process one can select certain parts of the sharia, and that parts exist which lend themselves to adaptations for the modern environment.

A conflict between Western legal thinking and the sharia?

Second question: is a Western court, or one influenced by Western legal thinking, inappropriate for the enforcement of the sharia? If so, are these cases instances of secular, Western-style courts dominating and overturning it? This is a particularly sensitive issue as a result of some (to Islamic law scholars) notorious statements in early oil-related arbitrations. "[I]t would be fanciful to suggest that in this very primitive region there is any settled body of legal principles applicable to the construction of modern commercial instruments." (Lord

Asquith in *Sheikh of Abu Dhabi v Petroleum Development (Trucial Coast) Ltd* 18 ILR 144 at 149, [1951] ICLQ 247 at 251.) "I need not set out the evidence before me about the origin, history, and development of Islamic Law as applied in Qatar or as the legal procedure in that country. I have no reason to suppose that Islamic Law is not administered there strictly, but I am satisfied that the law does not contain any principles which would be sufficient to interpret this particular contract." (Sir Alfred Bucknill in *Ruler of Qatar v International Marine Oil Co* (1953) 20 ILR 534 at 545.) "Saudi law must be interpreted or supplemented by the general principles of law, by the custom and practice in the oil business, and by notions of pure jurisprudence." (*Saudi Arabia v Aramco* 27 (1963) ILR 117.)

In the UAE assignments case, the issues of adaptation and conflict are linked. If it was true that the court was confronted with a truly unsquarable circle, the square being the secular law which reflects the perceived needs of modern commerce, the circle being the sharia, one might argue that the choice of secular law was determined by the Western influenced mentality of the Egyptian judges, for the Egyptian position in this area is based on French law and contains a provision for the transfer of a right (Arts 303 and 315 Egyptian Civil Code), and that this choice demonstrates that, even in an islamicising Muslim-majority jurisdiction such as the UAE, Western legal mentality is so dominant that the true sharia cannot survive.

However, if, following the suggestion put forward above, we accept that there was no such thing as "*the* classical *hawala*", but numerous *hawala*s, and that, among the Hanafis at least, rights were transferable, we can argue that the result of the case was not out of line with at least some of the classical law as practiced (raising, incidentally, the difficult question of whether modern law based on the sharia should reflect custom and stratagems, or whether it should be "cleansed" of such elements). The principle of *takhayyur*, or choice of one school's solution for the needs of the modern world, can then be applied to make it "the" modern sharia rule. (This reasoning would justify modern scholars' lack of concern in this area; they assume that such transfers are possible and concentrate on the issue of *riba*, see, eg, *M Aslam Khaki v Syed Muhammad Hashim* PLD 2000 SC 225 at 317 (Order of the Court).) In addition, one needs to bear in mind that the subject is so obscure that it might be said that it is not of particular cultural importance (Foster, "An Unstoppable Force", p 188).

In the *Affin Bank* case the issues of adaptation and conflict are also linked, for the adaptation produces a conflict with secular law ideas. A judge whose mentality is influenced by Western law refuses to enforce a contract of a type approved by sharia scholars. It is submitted, however, that here too the conflict is more apparent than real, and that, following the argument in the previous section on this case, the better view is that the judge was doing no more than exercising his sense of fairness, that he was quite right to do so, and that the true problem is the perfectly natural and inevitable one of adjustment. It is also submitted that there is an assumption underlying the "conflict" view, ie that a contract type approved by Islamic scholars must be perfect. This assumption is of course mistaken, as no drafter or reviewer of any legal mechanism can foresee all the consequences which may result from the use of that mechanism.

Beximco is perhaps the trickiest of the cases in this regard. We have already seen that it has been welcomed in the international financial community. Banks can get their money back (so long, of course, as they can enforce the judgment, but that is another story). However, one might argue that the sharia nature of the contract was ignored by the Court of Appeal. One might also argue that it was "anti-sharia" in the sense that it gave too much weight to the submissions concerning the uncertainty of the sharia because, as discussed previously, there is a considerable degree of consensus in Islamic finance, and that it was therefore wrong not to have accepted the incorporation argument. Here we enter a difficult area. The defendants' position was extremely weak, because it was clear that the Islamic nature of the transaction was irrelevant to them. This was explicitly mentioned in the judgment:

> *it is not uncommon for banks, in their enthusiasm to make profitable loans, to use a Morabaha Agreement to disguise what is, as a matter of commercial reality, an interest-bearing loan. That is precisely what happened in the present case and both the Claimant and the Defendants were quite content that this should happen. Neither was under any illusion as to the commercial realities of the transactions, and the claimant was happy to dress the loan transactions up as Morabaha sales (or Ijarah leases), whilst taking no interest in whether the proper formalities of such a sale or lease were actually complied with. (para 28.)*

Therefore their attempt to escape liability by claiming that its Islamicity was essential was viewed in a dim light. In addition, the hearing and the appeal therefrom concerned an application for a default judgment, which meant that the case proceeded on the basis of certain assumptions which would have been contested had the issues gone to a full trial.

As for the future, the agreed interpretation of the Rome Convention to the effect that its wording excluded the sharia as a governing law, requiring counsel for the defendants to argue that it should be incorporated by reference, meant that the issue of certainty was decisive as to whether the sharia could be applied. However, the relevant text is being revised as part of its transformation into an EU Regulation, and the draft wording contemplates the application of a non-state law, so long as it is precise enough:

> *To further boost the impact of the parties' will, a key principle of the Convention, [draft Article 3] paragraph 2 authorises the parties to choose as the applicable law a non-State body*

of law. The form of words used would authorise the choice of the UNIDROIT principles, the Principles of European Contract Law or a possible future optional Community instrument, while excluding the lex mercatoria, which is not precise enough, or private codifications not adequately recognised by the international community. Like Article 7(2) of the Vienna Convention on the international sale of goods, the text shows what action should be taken when certain aspects of the law of contract are not expressly settled by the relevant body of non-State law". (Commission of the European Communities (2005) "Proposal for a Regulation of the European Parliament and the Council on the Law Applicable to Contractual Obligations (Rome I) COM(2005) 650 final, p 5.)

Draft Article 3, paragraph 2 reads:

The parties may also choose as the applicable law the principles and rules of the substantive law of contract recognised internationally or in the Community.

However, questions relating to matters governed by such principles or rules which are not expressly settled by them shall be governed by the general principles underlying them or, failing such principles, in accordance with the law applicable in the absence of a choice under this Regulation.

In other words, if the same issue had to be decided on the basis of the new draft wording, it would be arguable that the sharia is applicable, but the issues of certainty and the impossibility of applying two laws would remain.

Perhaps more importantly, the governing law clause in question was an attempt to produce demonstrably Islamic transactions during an early stage of the development of Islamic finance law, an attempt which naturally explored only one of various available possibilities. Others which could be investigated include the designation of a national law such as that of Saudi Arabia, and the use of English law combined with the incorporation by reference of a specified sharia regime, whether national or determined by reference to standards such as those of the organisations already mentioned.

In addition, a choice of Islamic Law may well be recognised before an arbitral tribunal. According to one author: "A choice-of-law clause in favour of 'Islamic law' [...] is valid and workable, as long as the dispute is submitted to arbitration" (Bälz, K (2001) "Islamic Law as Governing Law under the Rome Convention. Universalist Lex Mercatoria v Regional Unification of Law" (NS 6) *Uniform Law Review* 37, p 44, citing Art 28(1) UNCITRAL Model Law). As regards arbitration in England, section 46(1)(b) Arbitration Act 1996 seems to allow the recognition of Islamic law: "The arbitral tribunal shall decide the dispute [...] if the parties so agree, in accordance with such other considerations as are agreed by them"). However, arbitration is not well suited to financial disputes, as it can take much longer to reach a conclusion than litigation in the English courts, can be more expensive, and does not benefit from the same range of remedies.

An approach adopted by one leading law firm is of considerable interest. The Islamicity of the contract is treated as a matter of compliance, rather than substantive law. In their documentation, which is of course approved by sharia scholars, the recitals state that the sharia is to be observed, and the bank's customer makes a representation that the customer is satisfied that the contract is Islamic (information from Neil Miller of Norton Rose in a conversation on May 2, 2006). This method ensures that the documentation meets sharia requirements by taking advantage of the English law principle of freedom of contract, which allows the construction of Islamically valid transaction structures and provides access to the advantages of the English court system, giving financial institutions effective and reasonably quick remedies. At the same time, it creates a situation in which it would be difficult for the customer to argue before an English court that sharia issues should be considered by the court, thus avoiding the sort of difficulties experienced by the Court of Appeal in *Beximco*, caused by their understandable unfamiliarity with Islamic finance law. Whether the approach achieves an Islamically proper result is difficult to say, as this depends on one's definition of "Islamically proper", but it does provide an interesting example of an attempt to respect sharia requirements while at the same time making litigation before a secular court as simple as possible.

The existence of this range of possibilities shows that, despite the Court of Appeal's possibly mistaken view of sharia certainty, English law is flexible enough to produce several possibilities for accommodation between the two systems.

CONCLUSION

It is submitted, therefore, that the answers to the question posed at the beginning of the previous sub-sections are: No and No.

No: the sharia is not inherently unsuitable for the modern commercial world, even if the process of adaptation is not yet complete.

No: with the possible exception of the UAE assignment case, the decisions discussed herein do not constitute instances of secular, Western-style courts dominating and overturning the sharia. There is no inherent or insoluble dichotomy between the sharia as it concerns financial transactions and Western-based legal systems.

However, this is not the end of the story.

On the adaptation point, if it is correct that the adaptation process is more difficult than initially realised, controversy and vigorous debate will no doubt result for, unlike Western law, issues relating to the sharia, an integral part of the Muslim religion, arouse strong emotions. For

example, the submission made above that Al-Bai Bithaman Ajil may not automatically be Islamic as a result of its approval by sharia scholars is controversial and emotive, surprising as this may seem to a Western-trained lawyer.

On the conflict point, if a secular, say, English, court did find itself in the position of having to enforce the sharia, whether as the governing law of the contract (if this is made possible by the revised Rome Convention), or as a set of rules incorporated by reference, various issues would arise.

Would it be viewed as desirable that a Western-trained judge decide a case with no knowledge of the sharia other than that given to her by expert witnesses? The point was made by Morison J in *Beximco*: "The English court, as a secular court, is not suited to ascertain and determine highly controversial principles of a religious-based law and it is unlikely that the parties would be satisfied by any such ruling; that is not what they were wanting by their choice of law clause" (para 36). He also stated that, if the sharia were effectively incorporated into the agreements, the court would be obliged to: "determine [a] dispute as to the nature or application of [...] controversial religious principles which would involve it in the task of deciding between opposing points of view which themselves might be based on geopolitical and particular religious beliefs" (paras 49–54, cited in para 40 of Potter LJ's judgment). (However, one should also recall the difference between those parts of the sharia relating to ritual and general behaviour (*ibada* and *akhlaq*) and that part relating to transactions (*mu'amalat*).)

Would such a situation result in the creation of an "English law financial sharia", along the lines of the much criticised Anglo-Muhammadan law of British Empire days? For example, if a secular court were to find, concerning facts similar to those of *Beximco*, that the agreement did not comply with the sharia, it would have to determine the effect of the resulting invalidity. In so doing, it would effectively create a form of persuasive precedent on the point (it could not formally have this effect, of course, since the decisions of an English court cannot affect non-English law). Would this be viewed as desirable? The considerations arising in a jurisdiction such as Malaysia are, of course, significantly different, as are the possible solutions, but nonetheless raise questions in the same sort of general area.

We can see, therefore, that although the apparent problems of adaptation and conflict are actually not anywhere near as serious as they might appear at first glance, the relationship between the sharia and secular law is far from settled, and will be one of the most interesting and significant topics for legal studies over the course of the next few decades.

Some further reading

Companion studies: Foster, NHD (Forthcoming) "Islamic Finance as an Emergent Legal System" *Arab Law Quarterly* (some of the material herein is shared with the material in that piece; for the sake of brevity, this is the only acknowledgement of that fact); Foster "An Unstoppable Force".

Islamic finance: Vogel, F E and Hayes, S L (1998) *Islamic Law and Finance: Religion, Risk and Return,* Kluwer Law International.

The "restoration" of the shari'a: Hallaq, WB (2004) "Can the Sharia Be Restored?" in Haddad, YY and Stowasser, BF (eds) *Islamic Law and the Challenges of Modernity* AltaMira Press.

Islamic finance regulatory bodies: Henry, CM (2005) "Introduction" in Ali SN (ed) *Islamic Finance: Current Legal and Regulatory Issues* Islamic Finance Project, Islamic Legal Studies Program, Harvard Law School at 4-5; Smith "Islamic Banking and the Politics of International Financial Harmonization", pp 172–77 (on the genesis of AAOFI) and pp 184–85 (on the IIFM and the LMC).

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