

# 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

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*“Are ye requited aught save what ye used to earn?”<sup>1</sup>*

## INTRODUCTION

The contemporary practice of Islamic banking and finance (“Islamic finance”) is a burgeoning yet immature niche within the global financial industry. Islamic finance can be set apart from conventional finance as much due to its unique and sophisticated theoretical underpinnings, as to what the modern financial complex would view as peculiarities or idiosyncrasies. Those characteristics, combined with the fact that Islamic finance exists in a world in which finance and religious sensibilities<sup>2</sup> rarely con-

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It is our humble hope that this Article may contribute to the body of literature proving that the accusation of unprincipled lawmaking in Islam has more to do with the plight of Islam in the modern world, namely the intellectual errors of the Islamic world in dealing with modernity, rather than any organic element of Islamic jurisprudence.

1. THE QUR’AN 10:52 (Marmaduke Pickthall trans., 1930).

2. We use the expression “religious sensibilities” as distinguished from “ethical sensibilities” because the modern world has no shortage of recourse to what it calls ethics. That ethics can be divorced from a religious context is implausible from the point of view of Islamic wisdom, and that it so thoroughly has been in the modern world, starting in and with the West, is cause for intellectual and moral alarm, not least among contemporary Western moral philosophers themselves. *See generally* ALASDAIR MACINTYRE, *AFTER VIRTUE* (2d ed. 1984) (discussing the need for a paradigmatic return to the will to virtue, the so-called way of Aristotle, in response to modernity’s and post-modernity’s destruction of any moral fabric other than the self-serving and inherently immoral will to power, the so-called way of Nietzsche, which is none other than rational self-egoism); *cf.* HENRY VEATCH, *HUMAN RIGHTS: FACT OR FANCY?* (1985) (comparing and contrasting the possibilities and consequences of basing a moral and legal regime

verge, can challenge and inspire both lawyers and financiers.

Despite the difficulties due to current associations of Islam with terrorism, Islamic finance continues to grow. Over the last three decades, Islamic finance has grown to involve over three hundred financial institutions in both Muslim countries and international financial markets including well over US\$200 billion in managed assets.<sup>3</sup> Many observers estimate current growth rates to be as high as fifteen percent per annum.<sup>4</sup> The industry is so young, however, that there is no reliable authoritative source that might record and track those statistics, which have been quoted for years throughout the Islamic finance world. As with any emerging market — especially one that may boast uniquely of over fourteen centuries' worth of jurisprudential and intellectual treasury — the potential for further quantitative and qualitative growth of Islamic finance *vis-à-vis* the global finance industry reflects a sense, at least among Muslims, of cautious optimism.

While the practice of Islamic finance has been a growing niche within the modern financial complex (and, thus far, not truly independent of it), its growth has not been accompanied by the emergence of a coherent body of governing rules and regulations native to the Islamic intellectual perspective. The Islamic financial institution, typically Western in its organizational form and collective outlook, and the Shari'ah committee that serves to provide Islamic legitimacy to the Islamic financial institution,<sup>5</sup> are both newly emerging constructs that have been

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on the first principles of either the will to power or the will to virtue, and insisting that the only way a proper basis can ever be found for laws, values and ethics is by explicit recourse to an objective reality, which is none other than the Divine Reality as manifested in the nature of things).

3. See Rodney Wilson, *The Evolution of the Islamic Financial System*, in ISLAMIC FINANCE: INNOVATION AND GROWTH 29 (Rifaat Abdel Karim & Simon Archer eds., 2002); see also The Institute of Islamic Banking and Insurance, Status of Islamic Banking, at <http://www.islamic-banking.com/ibanking/>.

4. See FRANK E. VOGEL & SAMUEL HAYES, ISLAMIC LAW AND FINANCE: RELIGION, RISK AND RETURN 5-6 (1998) (discussing generally the growth of the Islamic financial industry).

5. Typically, each Islamic financial institution hires, retains, and pays the salary of a committee of Islamic jurists to issue *fatwas* [non-binding opinion] declaring each transaction in which the institution engages to be permissible according to Islamic law. Such a committee is typically known as the Shari'ah committee. Before issuing its *fatwa*, the Shari'ah committee usually assists the financial institution by instructing it as to how to modify the transaction documents so that the transaction is not un-Islamic. The Shari'ah committee awards its mark of compliance to transactions that it deems accept-

given scant attention.<sup>6</sup> Islamic finance has developed along these lines because it has no status independent of its rival conventional finance. Indeed, Islamic finance inhabits a world as the weaker, but in symbiosis with its dominant rival, conventional finance. The economics and financial technology underlying Islamic finance are none other than those of the modern financial complex. In spite of the heavy influence of conventional finance on Islamic finance, there remains a hiatus of understanding between those who are engaged in Islamic finance and those who are not.

Many observers have likened Islamic finance to ethical finance. Ethics in the modern day tends to be divorced from religion.<sup>7</sup> In contrast, Islamic finance remains closely tied to the Islamic religion and, in large part, is founded on Muslims' attempts to live according to the Divine Will as evident in the Shari'ah. From a modern finance perspective, the principal difficulty in understanding Islamic finance is understanding what it means for finance to be based in religion. A practical question yet to be systematically addressed by Western regulators and academicians is how Western financial and legal systems should deal with the unique concerns and regulatory framework brought to bear by Islamic finance.

Islamic finance has just begun to grapple with the application of Islamic law to modern circumstances such as contemporary business entities<sup>8</sup> and how to address present-day commer-

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able. Too often, in our experience, the *fatwa* issued by the Shari'ah committee is exceedingly brief, containing only conclusory statements on mere components of the transaction. Astoundingly, there are no more than a dozen individuals serving in one capacity or another, on nearly every Shari'ah committee of every Islamic financial institution worldwide. The issue of whether there exists a conflict of interest in this arrangement is only now beginning to receive treatment.

6. Do banks, as we understand them, exist under Islamic law? Is the concentration of wealth in the hands of a few which might result from a "culture of banks" an acceptable phenomenon in Islam? Those are just some questions rarely asked in Islamic banking circles. In contemporary practice, an Islamic bank, like a conventional bank, acts as an intermediary and a trustee of other people's money. Unlike a conventional bank, however, the typical Islamic bank purports, as least in theory, to share profits and losses with its depositors. Though it may seem that profit- and loss-sharing introduces an element of mutuality, most Islamic banks, especially the larger ones, are organized much in the same way as their conventional corporate counterparts, i.e., with stratified stakeholders, and not as mutuals.

7. See *supra* note 2 (noting the disconnect between ethics and religion).

8. See IMRAN AHSAN KHAN NYAZEE, *ISLAMIC LAW OF BUSINESS ORGANIZATION: PARTNERSHIPS* (1999) (discussing from an Islamic legal perspective the theoretical underpin-

cial practices from an Islamic point of view.<sup>9</sup> For Islamic thought, in general, there is no question that the principles of Islam differ starkly from those of the modern West,<sup>10</sup> and those differences are no less evident when confining oneself simply to a comparison of modern legal and financial systems to Islamic finance. Those differences manifest themselves on the moral and legal planes where Islamic finance strives, first, to engage in transactions that do not contravene the substantive limits of the Shari'ah, and second, to promote the universal principle of economic fairness.<sup>11</sup>

Islamic finance has not come to terms with how best to go about functioning in a regulatory framework dominated by another legal system with its own financial technology. In fact, Is-

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nings of modern partnership forms); *see also* IMRAN AHSAN KHAN NYAZEE, *ISLAMIC LAW OF BUSINESS ORGANIZATION: CORPORATION* (1999) (discussing from an Islamic legal perspective the theoretical underpinnings of the modern corporation).

9. The Islamic legal process may validate custom [*urf*] so long as certain conditions are met. Foremost amongst those conditions is that the custom be a prevalent practice, reasonable and acceptable to people of sound nature, and consistent with the texts [*nusus*]. Many scholars employ custom in the interpretation of the Qur'an and the *hadith*, and also in issuing *fatwas*. For instance, whether a buyer of a defective good has the right to return the good is based upon the prevailing custom of the community where the sale has taken place. *See* MOHAMMAD HASHIM KAMALI, *PRINCIPLES OF ISLAMIC JURISPRUDENCE* 283-95 (rev. ed., Islamic Texts Soc'y 1991) (1989). *See also* SEYYED HOSSEIN NASR, *THE HEART OF ISLAM: ENDURING VALUES FOR HUMANITY* 121 (2002) (positing that custom or habit, whether mercantile or otherwise, is considered valid in the Shari'ah itself if such a custom or habit does not contradict or contravene the Shari'ah). *See also* Abdul Hakim & Sherman Jackson, *Jihad in the Modern World*, 1 *SEASONS* 31, 35 (Spring/Summer 2003) (quoting the esteemed jurist al-Qarafi (d. 1285) who stated: "Holding to rulings that have been deduced on the basis of custom, even after this custom has changed, is a violation of Unanimous Consensus ('*ijma*') and an open display of ignorance of the religion"). *See also id.* at 35 (quoting the Fifth Session of the Islamic Law Academy of the Organization of the Islamic Conference: "No jurist, neither as judge, nor as an issuer of non-binding opinions ('*fatwa*'), may restrict himself to that which has been handed down in the manuals of the classical jurists, failing in the process to pay adequate attention to changes in custom").

10. *See generally* SEYYED HOSSEIN NASR, *KNOWLEDGE AND THE SACRED* 81-86 (1989). Ultimately, this resolves to less a question of modernity and the way of Islam, and more a question of modernity *vis-à-vis* all of known human tradition. *See generally*, RENE GUENON, *THE REIGN OF QUANTITY AND THE SIGNS OF THE TIMES* (Lord Northbourne trans., Luzac & Co., Ltd. 1953) (1930).

11. *See* NASR, *supra* note 9, at 144-47. Before modern times, economics and economic law in Islam were always combined with ethics and were understood as being an organic part of the life of human beings, all of which should be dominated by ethical principles. "[I]n fact, the modern Arabic word for economics, *al-iqtisad* [used to have] the completely different meaning of 'moderation' or the 'just mean' in classical Arabic." *Id.* at 144. *See generally* M. UMER CHAPRA, *ISLAM AND THE ECONOMIC CHALLENGE* (1992).

lamic finance now operates at a time when the Shari'ah is not integrally practiced and enforced wholly as the law in any country. To exacerbate the problem, bankers and practitioners in Islamic finance, often trained solely in modern finance and banking methods, lack any traditional education and therefore, lack any legitimate knowledge of Islamic law. On the other hand, Shari'ah committee members, while educated in Islamic law and jurisprudence, are not usually educated in modern finance and economics. Thus, an intellectual barrier separates the two groups that must meld in order for the challenges facing Islamic finance to be properly addressed.

Islamic financial regulation, in its classical formulation, comprised a plethora of schools of thought and positions on any given legal or jurisprudential issue, and Islamic scholarship as a whole celebrated such divergence of opinion.<sup>12</sup> With a backdrop of a multiplicity of interpretations within Islam,<sup>13</sup> the guardians of the outward expression of Islam were the jurists [*fuqaha*'], and the guardians of the inward tradition were the spiritual masters. Both the inward and outward aspects of Islamic teaching have had their rightful place in Islam, and more often than not, both these aspects have been integrated and present in one and the same person.

This Article focuses on the case of *Islamic Investment Company of the Gulf (Bahamas) Ltd. v. Symphony Gems N.V. & Others*<sup>14</sup> (“Sym-

12. Four orthodox schools of Islamic law and jurisprudence survive to the present day in the Sunni tradition: the Hanafi, Maliki, Shafi'i and Hanbali. In contrast to the Sunni tradition, there is the Shi'ah tradition of Islamic thought, which comprises its own schools of law and jurisprudence, the most notable being the Ja'fari. Only the Sunni schools of law and jurisprudence are discussed in this Article. For more information concerning the schools of Islamic legal reasoning in the Sunni world, see GEORGE MAKDISI, *THE RISE OF COLLEGES: INSTITUTIONS OF LEARNING IN ISLAM AND THE WEST* (1981) and CHRISTOPHER MELCHERT, *THE FORMATION OF THE SUNNI SCHOOLS OF LAW, 9TH-10TH CENTURIES C.E.* (1997). See also, KHALED ABOU EL FADL ET AL., *THE PLACE OF TOLERANCE IN ISLAM 6* (Joshua Cohen & Ian Lague eds., 2002) (stating “[t]raditionally, Islamic epistemology tolerated and even celebrated divergent opinions and schools of thought”).

13. A comparison of the different opinions among schools and scholars leads inevitably to a discussion of dispensation and strictness. Dispensation is found where a particular school's ruling on a matter is easiest to implement and strictness is found where it is difficult to implement. Traditional scholars of Islamic law and philosophy acknowledged that the differences among schools constituted a mercy on Muslims. See AHMAD IBN NAQIB AL-MISRI, *RELIANCE OF THE TRAVELER: A CLASSIC MANUAL OF ISLAMIC SACRED LAW* 38 (Nuh Ha Mim Keller trans., 1994).

14. 2002 WL 346969 (Q.B. Com. Ct. Feb. 13, 2002).

*phony Gems*”). *Symphony Gems* is the first instance where a Western court of law ruled on an Islamic financial transaction. *Symphony Gems* illuminates the challenges and tensions within the industrial complex of Islamic finance as it seeks to exist and thrive in a commercial reality where the regulatory framework and its associated assumptions (both theoretical as well as those of commercial practice) differ markedly from those of Islamic law and the contemporary Islamic financial industry. The resulting transactions often deviate from the classical modes or forms upon which they are supposed to be based. From a conventional finance perspective, Islamic transactions can be criticized as being anomalous, inefficiently structured and obliquely documented.

*Symphony Gems* arose out of the applicability of an Islamic financial contract known as a *murabahah*.<sup>15</sup> This Article will explain both the conceptual basis and the contemporary usage of the *murabahah* contract and, more generally, the challenges of integrating Islamic financial concepts into the Anglo-American legal system that predominates the modern global economy. *Murabahah* contracts, simply stated, involve the sale of an item, through a middleman, in which the ultimate buyer is aware of the middleman’s costs in obtaining the item.<sup>16</sup> As discussed later

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15. *Murabahah* is often defined as “cost plus mark-up sale.” We have elected to utilize the Arabic term in this Article not only because this translation would be cumbersome, but also because we do not believe any translation of which we know fully and adequately expresses the Islamic legal concept.

16. See, e.g., J. Michael Taylor, *Islamic Banking — The Feasibility of Establishing an Islamic Bank in the United States*, AM. BUS. L.J. 385, 395-96 (2003). Taylor explains that

[i]n a typical *murabahah* transaction, the financial institution acts as a middleman and purchases a good requested by its customer; the financial institution then turns around and sells the good to the customer at the acquisition cost plus a profit. The customer agrees to pay for the good over a stated period in installments, but if there is a default (unlike in traditional financing) the customer is only liable to the financial institution for the contracted sale price (not any fees or interest calculations otherwise available in typical financing arrangements).

A key component of *murabaha* [sic] financing is the requirement that the financial institution actually own the good before transferring title to its customer. This is because the financial institution assumes some risk to justify its profit, making the profit more than just disguised interest. The customer could always refuse to accept the good obtained for it by the financial institution, causing the financial institution to find an alternative buyer with the accompanying costs of storage, marketing and overhead.

*Id.*

The problem with Taylor’s description, however, is that it reveals a transaction that

in this Article, *murabahah* contracts in contemporary practice closely approximate conventional financing mechanisms, particularly the economics underlying a similarly-profiled conventional commercial financing. This is why *murabahah* contracts are so popular.<sup>17</sup> Therefore, it is not surprising that the first instance in which a Western court of law has examined and opined upon an Islamic financial contract involves a *murabahah* sale.

## I. ISLAMIC FINANCE VIS-À-VIS CONVENTIONAL FINANCE

### A. A Brief Word on Conventional Finance

Over the course of the last three decades, conventional finance has witnessed both an unprecedented tide of new instruments and techniques and a wide expansion across international borders. Conventional finance or modern finance — we use these two expressions interchangeably — is “conventional” because it is the financial and banking order that today dominates the world scene. This dominance is a result of, first, the colonial and military encroachment on the remainder of the world by Western European and, later, American powers, and, second, the late twentieth century occurrence of globalization. Though the assumptions of conventional finance relating to man and nature differ from those of any other financial system with which it came into contact, in practice the dominated have had little success in countering those assumptions. The march toward global financial integration — replacing culturally distinct, organic systems with the modern system — has not sidestepped the Islamic world, and the latter decades of the twentieth century have seen in the very heart of the Islamic world the emergence of Western-style financial institutions which participate *carte blanche* in the modern financial complex.

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does not comport with the elements of a *murabahah* as practiced in contemporary Islamic finance.

17. See ABDULLAH SAEED, *ISLAMIC BANKING AND INTEREST: A STUDY OF THE PROHIBITION OF RIBA AND ITS CONTEMPORARY INTERPRETATION* 77-78 (1996) (noting that “Islamic banks in general have been using *murabahah* as their major method of financing, constituting approximately seventy-five percent of their assets”); accord Humayon A. Dar & John R. Presley, *Lack of Profit Loss Sharing in Islamic Banking: Management and Control Imbalances*, 2 INT’L J. OF ISLAMIC FIN. SERVICES 1, 1 (July-Sept. 2000), available at <http://islamic-finance.net/journals/> (stating that “[A]most all theoretical models of Islamic banking are either based on *Mudaraba[h]* or *Musharaka[h]* or both . . . . Nearly all Islamic banks, investment companies, and investment funds offer trade and project finance on mark-up, commissioned manufacturing, or on leasing bases”).

Nevertheless, Muslims did not wish to completely reject the native elements of Islamic civilization and it did not take long for Muslims to develop financial practices purporting to be at once compliant with Islamic law and jurisprudence and workable within the rubric of conventional banking and finance. This immense task of taking fourteen centuries' worth of legal scholarship and conforming it within a brief span of time — barely two decades — and with limited intellectual resources, to accord with a system completely alien to it came about by contemporary jurists massaging certain classical modes or forms of Islamic transactions to arrive at what Professor M. A. El-Gamal has referred to as the “closest permissible point,” the unique tangency between what contemporary jurists view as permissible under Islamic law and what conventional finance views, according to its own terms, as efficient or optimal.<sup>18</sup> It is because Islamic finance has bowed to the norms of conventional finance that purveyors of conventional finance see Islamic finance as no more than a niche within the modern financial complex, where, for them, marginal revenues are waiting to be made. Seen from this point of view, the question whether there is more to Islamic finance than the foregoing need not be asked.

### B. *Islamic Finance within the Context of Islam*

A great deal of confusion will be allayed if it is acknowledged at the outset that in Western discussions of Islam, the term is used interchangeably to denote both the religion [*din*] of Islam<sup>19</sup> and the civilization of Islam.<sup>20</sup>

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18. See Mahmoud A. El-Gamal, *The Economics of 21st Century Islamic Jurisprudence*, Speech at the Fourth Harvard University Forum on International Finance (Oct. 2000), at <http://www.ruf.rice.edu/~elgamal/files/islamic.html>.

19. As a religion,

Islam is the meeting between God as such and man as such. God as such: that is to say God envisaged, not as He manifested Himself in a particular way at a particular time, but independently of history and inasmuch as He is what He is and also as He creates and reveals His nature. Man as such: that is to say man envisaged, not as a fallen being needing a miracle to save him, but as man, a theomorphic being endowed with an intelligence capable of conceiving of the Absolute and with a will capable of choosing what leads to the Absolute.

FRITHJOF SCHUON, *UNDERSTANDING ISLAM I* (1994).

Professor Nasr, discussing the religion of Islam states:

At the heart of Islam stands the reality of God, the One, the Absolute and the Infinite, the Infinitely Good and All-Merciful, the One Who is at once transcendent and immanent, greater than all we can conceive or imagine, yet, as



One cannot speak of Islamic finance without speaking first of Islamic law and jurisprudence. This is because Islam countenances living every aspect of one's life in accordance with norms laid down by God.<sup>21</sup> As a comprehensive view of life both in relation to this world and the Hereafter,<sup>22</sup> Islam integrates material and spiritual aspects of human beings in accordance with Divine principles. The Shari'ah<sup>23</sup> — frequently translated as “Islamic law” or “Divine Law” — constitutes a web of beliefs, values, and guidelines meant to establish and maintain human life in this world in balance with the realities that exist beyond the temporal order.<sup>24</sup> The injunctions of the Shari'ah are permanent,

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the Qur'an, the sacred scripture of Islam, attests, closer to us than our jugular vein.

NASR, *supra* note 9, at 3.

In this Article, when the religion [*din*] of Islam is meant, the term “Islam” alone is used. When the civilization of Islam, the world of Islam or the human community of Islam is meant, the expression “Islamic world” or “Islamic civilization” is used. The adjective “Islamic” connotes something relating to either the religion or the world of Islam. The term “Muslim” is a noun that refers to an individual follower of Islam, and when used as an adjective, “Muslim” refers to something pertaining to the followers of Islam, not to the religion or world of Islam.

20. As a civilization or human community, “[t]he vast world of Islam is actually like a Persian medallion carpet; it has incredible diversity and complexity, yet it is dominated by a unity into which all the complex geometric and arabesque patterns are integrated.” NASR, *supra* note 9, at 57. For more information about the perspectives within Islamic civilization, see SEYYED HOSSEIN NASR, *SCIENCE AND CIVILIZATION IN ISLAM* 29-40 (1968).

21. For a general introduction to Islam, see ROGER DUPASQUIER, *UNVEILING ISLAM* (T.J. Winter trans., 1992); SUZANNE HANEEF, *WHAT EVERYONE SHOULD KNOW ABOUT ISLAM AND MUSLIMS* (1979); SCHUON, *supra* note 19; NASR, *supra* note 9.

22. For a discussion of the concept of the “Hereafter,” see generally ABU HAMID AL-GHAZALI, *THE REMEMBRANCE OF DEATH AND THE AFTERLIFE* (T.J. Winter trans., 1989).

23. Literally, the word “Shari'ah” means “the road to the watering place or path leading to the water, i.e., the way to the source of life.” Irshad Abdal-Haqq, *Islamic Law: An Overview of its Origin and Elements*, 1 J. ISLAMIC L. 1, 2 (1996). “The Shari'ah itself is a vast network of injunctions and regulations which relate the world of multiplicity inwardly to a single Center which conversely is reflected in the multiplicity of the circumference.” SEYYED HOSSEIN NASR, *SUFI ESSAYS* 43 (1999).

24. The terms “Islamic law” and “Shari'ah” are frequently used interchangeably in Western scholarship. It is an oversimplification, however, to equate the Shari'ah with law. The Shari'ah — which we have deliberately chosen not to translate in this Article — may be said to contain law, but one must also recognize that it embraces elements and aspects that are not, strictly speaking, law because they are beyond our conventional understanding of law. See BERNARD WEISS, *THE SEARCH FOR GOD'S LAW: ISLAMIC JURISPRUDENCE IN THE WRITING OF SAYF AL-DIN AL-AMIDI* 1 (1992).

One of the most difficult aspects of Islam for modern people to understand is the philosophy of law which reinforces the metaphysical basis for the Shari'ah in Islam. If modern people in the West were able to grasp what the Old Testament says about the

and the principles inherent in the Shari'ah can and ought to be applied to new circumstances — such as Islamic finance in the present day — as they arise.

The primary sources of the Shari'ah are the Qur'an<sup>25</sup> and the Sunnah.<sup>26</sup> The detailed practical rules derived by reasoning from the corpus of Shari'ah are known as *fiqh*.<sup>27</sup> Whereas the Shari'ah includes moral laws and the general framework for re-

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status of law or how traditional Jews in the present day comprehend and practice Talmudic Law, it would make it easier to grasp the philosophy of law in Islam. Indeed the Shari'ah and the *Halakhah* hold very similar positions in Islam and Judaism, respectively. NASR, *supra* note 9, at 117-18.

The Semitic conception, shared by both Judaism and Islam, sees law as the embodiment of the Divine Will, as a transcendent reality which is eternal and immutable, as a model by which the perfections and shortcomings of human society and the conduct of the individual are judged, as the guide through which man gains salvation and by rejecting it, courts damnation and destruction.

SEYYED HOSSEIN NASR, *ISLAMIC LIFE AND THOUGHT* 25 (1981).

25. See NASR, *supra* note 9, at 120. "The great theophany of Islam is the Qur'an; it presents itself as a 'discernment' (*furqan*) between truth and error." SCHUON, *supra* note 19, at 39. For Muslims, the Qur'an is the "the book containing the speech of God revealed to the Prophet Muhammad," peace be upon him. KAMALI, *supra* note 9, at 14.

The phrase "peace be upon him" is customarily said and written after mention is made of the Prophet Muhammad as well as all the other prophets, peace be upon them all. See ABU HAMID AL-GHAZALI, *INNER DIMENSIONS OF ISLAMIC WORSHIP* 129-32 (Muhtar Holland trans., n.d.).

The Qur'an contains approximately five hundred specific legal injunctions; for the most part, the Qur'an sets general guiding principles. See Abdal-Haqq, *supra* note 23, at 21; see AHMAD HASAN, *THE EARLY DEVELOPMENT OF ISLAMIC JURISPRUDENCE* 44-45 (4th ed. 1988). For a concise primer in English to the sciences of the Qur'an, see generally AHMAD VON DENFFER, *'ULUM AL QUR'AN: AN INTRODUCTION TO THE SCIENCES OF THE QUR'AN* (1989). For a brief introduction in English to the discipline of Qur'anic exegesis, see generally IBN TAYMIYYA, *AN INTRODUCTION TO THE PRINCIPLES OF TAFSEER* (Muhammad 'Abdul Haq Ansari trans., 1993).

26. "The word 'Sunnah' [sic] literally means 'a clear path or a beaten track,' 'a normative tradition,' 'habitual practice,' 'customary procedure or action,' 'or an established course of conduct.'" MICHAEL MUMISA, *ISLAMIC LAW: THEORY AND INTERPRETATION* 55 (2002). "In its juristic usage, Sunnah refers to the normative practice set up by the Prophet of Islam as a model; his sayings, doings, and tacit approvals which were later established as legally binding precedents in addition to the law established by the Qur'an." *Id.* at 56.

27. "*Fiqh*, according to traditional authorities, is knowledge of the practical regulations and rules of the Shari'ah acquired by reference to and detailed study of the sources." NASR, *supra* note 9, at 123. See ERIC WINKEL, *ISLAM AND THE LIVING LAW: THE IBN AL-ARABI APPROACH* 15 (1997) (positing that *fiqh* is the application of the Shari'ah to different times and places based on the deeply and vigorously debated rules and methodologies of *usul al-fiqh*).

The term *fiqh* is simply translated hereinafter and referred to throughout this Article as "Islamic law."

ligious life in Islam, *fiqh* refers to the *result* of the human activity of exploration, interpretation, analysis, and presentation of the textual sources of the Shari'ah, whether this takes place in writing, in schools, in the mind, or in formal opinion-giving.

*Usul al-fiqh*, literally the "roots of Islamic law," constitutes the science of deriving the detailed rules of Islamic law from their sources. In other words, *usul al-fiqh*, whether translated as "roots of Islamic law" or simply as "Islamic jurisprudence,"<sup>28</sup> comprises methods of reasoning and rules of interpreting which are applied to the texts of the Qur'an and Sunnah in order to deduce Islamic law. In comparison, Islamic law comprises the practical rules of the Shari'ah derived from detailed evidence in the textual sources, and is thus the end product of Islamic jurisprudence [*usul al-fiqh*]. Islamic law [*fiqh*] and Islamic jurisprudence [*usul al-fiqh*] are two entirely distinct disciplines.<sup>29</sup>

The goals and objectives of the Shari'ah are known in Arabic as *maqasid al-Shari'ah*.<sup>30</sup> Securing benefit and preventing harm in this life and in connection with the Hereafter are the most important considerations [*maslahah*] of Islamic law.<sup>31</sup> In order to prevent arbitrary or illogical results, jurists developed an elaborate and varied<sup>32</sup> set of conditions and procedures

28. See KAMALI, *supra* note 9, at 1. Cf. SHERMAN A. JACKSON, ISLAMIC LAW AND THE STATE: THE CONSTITUTIONAL JURISPRUDENCE OF SHIHAB AL-DIN AL-QARAFI 121 (1996) (translating the Arabic expression *usul al-fiqh* as "Islamic theoretical jurisprudence"). *Usul al-fiqh* has also been translated as "sources of legal discourse." See WINKEL, *supra* note 27, at 35.

29. See KAMALI, *supra* note 9, at 1. The exhaustion of one's mental capacity in the attempt to gain probable knowledge about anything concerning the Shari'ah may be understood as the process of *ijtihad*, which must only be conducted by one properly qualified to do so. See Sherman Jackson, *Taqlid, Legal Scaffolding and the Scope of Legal Injunctions in Post Formative Theory: Mutlaq and 'Amm in the Jurisprudence of Shihab al-Din al-Qarafi*, 3 ISLAMIC L. SOCIETY 165, 167 n.5 (1996) (quoting SAYF AL-DIN AL-AMIDI, AL-IHKAM FI USUL AL-AHKAM (1968)). Professor Jackson offers his own definition of *ijtihad* as "the interpretation of scripture directly with no intermediate authorities standing between the sources and the individual jurist." *Id.*; see also, KAMALI, *supra* note 9, at 366-93 (discussing the rigorous conditions required to be a *mujtahid*, one who conducts *ijtihad*).

30. See IMRAN AHSAN KHAN NYAZEE, THEORIES OF ISLAMIC LAW 237 (1994) (stating also that, according to al-Shatibi (d. 1388 C.E.), the purposes of the law have been inferred inductively from the texts).

31. See *id.* at 42-44 (commenting that there is a lengthy and rich discourse surrounding the ultimate intent of the law and the Lawgiver). See also NASR, *supra* note 9, at 121.

32. Varied because different thinkers arrived at different results depending upon their methodology in conducting *ijtihad*. It would not be uncommon for *mujtahids* who

which need to be fulfilled in order to permit reliance upon *maslahah* when arriving at a particular ruling.<sup>33</sup> In order for any rule of Islamic law to be valid and applicable it must not violate the ultimate intent and purpose of the Shari'ah.<sup>34</sup>

In addition to *maslahah* and *maqasid al-Shari'ah*, there exists the technical concept of ratiocination [*ta'lil*]<sup>35</sup> in Islamic jurisprudence which is a tool of legal reasoning employable when deriving Islamic law. *Ta'lil* literally means "causation" or "search for the causes" and refers to the rational<sup>36</sup> relationship between cause and effect. Although this is what *ta'lil* literally means, jurists have tended to use the term in the context of the ratio of the law, in other words, its operative value in causing a rule of law to spring into effect.<sup>37</sup>

When the discourse turns to the goals, objectives and value of the law, invariably one must also open the door to a discussion of letter and spirit, or form and substance. Every religion has a form and a substance, and Islam is no different in this regard.<sup>38</sup> Islamic jurisprudence provides methodological tools to investi-

used the same methodological approach — students of the same school of Islamic jurisprudence — to arrive at conclusions at odds with one another.

33. See KAMALI, *supra* note 9, at 273-75 (listing several important conditions for the use of *maslahah*). Most jurists classify *maslahah* into three categories each of which must be protected: (1) the *daruriyyat* [essentials], (2) the *hajiyyat* [complements], and (3) *tahsiniyyat* [embellishments]. See *id.* at 271. The *daruriyyat* consist of five essential interests: the preservation of *din* [religion], *nafs* [life], *'aql* [intellect], *nasl* [progeny], and *mal* [property]. The *hajiyyat* are those interests, the disregard of which result in hardship but not in the destruction or ruin of the community. See NYAZEE, *supra* note 30, at 214. Lastly, the *tahsiniyyat* are those interests "whose realisation leads to improvement and the attainment of that which is desirable." KAMALI, *supra* note 9, at 272. An example of such is cleanliness in personal appearance. See *id.* Every Islamic ruling aims at one of these three categories of objectives of the law.

34. See NYAZEE, *supra* note 30, at 222-23, 242.

35. For more information regarding the science of ratiocination [*ta'lil*] in Islamic jurisprudence, see MUHAMMAD MUSTAFA SHALABI, *TA'LIL AL-AHKAM* (1981) (in Arabic).

36. We use the descriptor "rational" because Islamic jurisprudence views relationships of cause and effect to be, other than rational, both supra-rational and infra-rational. Supra-rational when the relationship is above and beyond the domain of the rational faculty and knowable only in God's wisdom. Infra-rational when the relationship has a sentimental, emotional, or other irrational basis.

37. Moreover, it must be borne in mind that the authority of the Qur'an as the chief source of Shari'ah is fundamentally independent of ratiocination. Muslims are supposed to accept the plain injunctions of the Qur'an — there are very few of them so plainly stated — irrespective of whether such injunctions can be rationally explicated. See KAMALI, *supra* note 9, at 35.

38. See FRITHJOF SCHUON, *FORM AND SUBSTANCE IN THE RELIGIONS* 14 (2002) (stating "Islam spread like lightning by virtue of its substance").

gate and distinguish between the letter and rationale of Islamic law. Beside *ta'li'l*, one key method, among others, of dealing with the substance or spirit of Islamic law centers on the concept of *hikmah*. The *hikmah* of a rule of law is that law's ultimate objective as known in the Lawgiver's (i.e., God's) wisdom.<sup>39</sup>

It is easier to understand *hikmah* by contrasting it to its counterpart *'illah*, which is a term that shares a common linguistic derivation from the term *ta'li'l*. *'Illah* (plural *'ilal*) may be understood as the formal or effective cause, legally speaking, for the activation of a rule of Islamic law.<sup>40</sup> In practice, should a jurist wish to extend an existing rule of law, the jurist must establish a common *'illah* between the original case and the new case. If implemented correctly, the *'illah* causes the application of an existing ruling to a new situation, thereby creating new law, in order to establish, preserve, or protect a predetermined purpose of the law.<sup>41</sup> Functionally speaking, the *'illah* need not even look at the purpose of the rule of Islamic law, which, strictly speaking, lies in the province of *hikmah*. Nevertheless, the establishment, preservation or protection of a predetermined purpose of Islamic law follows the proper application of *'illah*.

The textual sources of the Shari'ah can explicitly state the *'illah* just as they can the *hikmah*. Unlike the *hikmah*, the *'illah* can be identified by jurists through *ijtihad*, as well as through logical or speculative reasoning.<sup>42</sup> Generally speaking, *hikmah* is not subject to rational inference, although jurists can apply it analogically if it is expressly set forth in the textual sources of the Shari'ah. If it is not expressed in the Qur'an or Sunnah, the *hikmah* of any given rule of law may still at times be the subject of jurist's reasoning and, if it is, the *probable hikmah* — probable rather than certain because the jurist reasoned it rather than discovered it plainly stated in the text — may be used substantively as an adduced source of general principles in expounding Islamic law. Islamic law and jurisprudence enjoy a greater treasury of technical methods and procedures than what we have space to

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39. See KAMALI, *supra* note 9, at 35.

40. See Umar F. Moghul, *Approximating Certainty in Ratiocination: How to Ascertain the 'Illah (Effective Cause) in the Islamic Legal System and How to Determine the Ratio Decidendi in the Anglo-American Common Law*, 4 J. ISLAMIC L. 125 (1999).

41. See NYAZEE, *supra* note 30, at 208.

42. See KAMALI, *supra* note 9, at 35.

mention here,<sup>43</sup> but for now, the foregoing exposition is sufficient to give the reader a taste of how Islamic law countenances law, its philosophy, its letter, and its spirit.

### C. *Two Categories of Islamic Law*

The Shari'ah has given rise to two bodies or categories of Islamic law which: (1) pertain to worship [*'ibadat*], and (2) govern human interactions and transactions [*mu'amalat*] which includes those areas that Anglo-American law would describe as contracts, torts, property law, and criminal law. This dual categorization mirrors the dual nature of humans as beings having, in the same instance, a temporal aspect and an aspect beyond time and space. Generally speaking, different rules govern the derivation and application of law in *'ibadat* and *mu'amalat*.<sup>44</sup> Jurists acknowledge that although the sources of Islamic law are divine, their derivation and application must be a construct of the human intellect. This is reflected in the epistemology of the legal reasoning that the jurists constructed.<sup>45</sup>

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43. For a more detailed exposition of Islamic law and jurisprudence than what can be provided within the limited confines of this Article, see generally KAMALI, *supra* note 9; MUMISA, *supra* note 26; NASR, *supra* note 9, at 113-56.

44. For example, according to the overwhelming majority of Islamic jurists, matters that fall within the realm of *mu'amalat*, such as financial transactions, are presumptively permissible under the Shari'ah unless determined otherwise by jurists. See MUHAMMAD HASHIM KAMALI, *ISLAMIC COMMERCIAL LAW: AN ANALYSIS OF FUTURES AND OPTIONS* 66-83 (2000). It should be noted, unsurprisingly, that the minority position holds that actions within the realm of *mu'amalat* are presumed impermissible under the Shari'ah unless Islamic law expressly permits them.

Thus, given the majority's presumption of permissibility, a misunderstanding looms when one opens a contemporary treatise on Islamic finance and reads a list of contracts and transaction forms which are claimed by the jurist as representing an exhaustive list of those forms acceptable under Islamic law. See, e.g., MUHAMMAD TAQI USMANI, *AN INTRODUCTION TO ISLAMIC FINANCE* (1999). The implication is that these dozen or so contracts and transaction forms constitute the sum total of what Islam offers or are all somehow *per se* divinely ordained. Consequently, many contemporaries assert — not verbally but rather through their hermeneutics and legal method — that for a transaction to be Islamic, it must fit within one of these preconceived contracts or combinations thereof. In undertaking this exercise, one often finds that the transaction results in something not entirely intended by the parties and or one that does not accord optimally with the Shari'ah and is, at the same time, somewhat of an oddity under local law. Yet Muslim jurists living in centuries past regularly commented that the enumerated forms of trading and transacting are not the only modes or forms permissible under Islamic law. It is very interesting to note that upon even a superficial study of the enumerated contract forms, one finds jurists historically permitted many of the contract forms as exceptions to various legal maxims and principles.

45. See, e.g., A. Kevin Reinhart, *When Women Went to Mosques: al-Aydini on the Dura-*

The principles and rules with respect to the *'ibadat* are constant and immutable and thus consistent with the spiritual nature of the human, which exists in this life and shall exist in the eternal life of the Hereafter.<sup>46</sup> The *'ilal* of acts of *'ibadat* are generally imperceptible to the human intellect, although the intellect may be able to intuit the higher purpose and value in the various acts of worship.<sup>47</sup> The *'ilal* of the *mu'amalat*, on the other hand, are discernible to the human intellect.<sup>48</sup> Thus, the guidelines pertaining to *'ibadat* are understood by jurists to be beyond reasoning whereas the guidelines pertaining to *mu'amalat* are subject to reasoning.<sup>49</sup> It suffices to say that, generally speaking, the legal rules of the *'ibadat* cannot necessarily be rationalized in the same manner as can those of the *mu'amalat*.<sup>50</sup> In contrast to the *'ibadat*, the *mu'amalat* constitute a mutable and dynamic body of law, pliable within the bounds of the Shari'ah to the existential and material realities of human life in this world. The *'ilal* of the *mu'amalat* are knowable by the rational faculty. In this way, human beings subject them to rational thought and juristic reasoning.<sup>51</sup>

One may take a functional approach in describing Islamic finance today, and observe that Islamic finance provides conventional financial services on a basis that complies with Islamic law and Islamic jurisprudence. Islamic financial instruments and transactions must, according to prevailing opinion in the industry,<sup>52</sup> take the form of one of the classically prescribed contracts.

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*tion of Assessments, in ISLAMIC LEGAL INTERPRETATION: MUFTIS AND THEIR FATWAS* 116 (Khalid Mas'ud et al. eds., 1996).

46. See Moghul, *supra* note 40, at 141-42.

47. *Id.* Islamic scholarship observes the difference between *intellectus* or *nous*, on the one hand, and *ratio* or reason, on the other. Muslim sages throughout the ages such as Abu Hamid al-Ghazzali and Jalal al-Din Rumi cautioned against the negative aspect of the rational faculty as a veil and limitation impeding one's ability to reach the divine verities. See NASR, *supra* note 23, at 52-56.

It should be noted that in the context of the *'ibadat*, the term *sabab* is often used instead of *'illah* to refer to the effective cause, or perhaps more precisely the effective condition of a rule of law. See NYAZEE, *supra* note 30, at 67 n. 13; see also KAMALI, *supra* note 9, at 211.

48. Moghul, *supra* note 40, at 142.

49. See 'ABD AL-KARIM ZAYDAN, *AL-WAJIZ FI USUL AL-FIQH* 57-58 (1967) (in Arabic).

50. See e.g., AL-MISRI, *supra* note 13, at 52-56 (discussing purities and impurities of water in the context of ablution).

51. See e.g., ZAYDAN, *supra* note 49, at 57-58; ABU ZAHRAH, *USUL AL-FIQH* 57-59 (1950).

52. See generally Yusuf Talal DeLorenzo, *The Religious Foundations of Islamic Finance*,

Jurists claim that the contracts commonly used in contemporary Islamic finance are basically the same as those used for centuries in the Islamic world, and for that reason, are acceptable to them and to the Islamic finance industry as *prima facie* appropriate. The desire for comportment of these contracts to the Anglo-American system of law — sometimes the comportment is forced, sometimes it is contrived — is a new phenomenon, the significance of which has not yet gripped either the Islamic finance world or the broader Islamic community. This Article posits that a disconnect is being propagated between, on the one hand, the spirit, wisdom and ultimate goals of the Shari'ah and, on the other, the form in which Islamic finance is packaging its products and services. This disconnect has reached a level of significance such that not only does Islamic financial literature recognize it,<sup>53</sup> but with the opinion handed down in *Symphony Gems*, so does a Western court of law.

#### D. Contractual Forms and Limitations within Islamic Law

This Article now focuses on a technical description of contractual forms in Islamic law.

##### 1. Contract Forms

The Shari'ah seeks to ensure propriety and fairness and to protect the integrity of mutual assent and the rights of contracting parties. In general terms and given the presumption of permissibility,<sup>54</sup> the Shari'ah entitles parties to stipulate the terms and conditions of their agreement so long as they do not violate the Shari'ah.

Contract formation<sup>55</sup> in Islamic law begins with certain human behavior or conduct [*tasarruf*], whereby persons create or agree upon a contractual right.<sup>56</sup> Jurists, in discussing the

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in ISLAMIC FINANCE: INNOVATION AND GROWTH 9-28 (Simon Archer & Rifaat Ahmed Abdel Karim eds., 2002).

53. See, e.g., El-Gamal, *supra* note 18.

54. See *supra* note 43 (citing sources for which to refer for a more detailed exposition of Islamic law and jurisprudence).

55. For a historical discussion of sales and contracts, see 'ABDULLAH 'ALWI HAJI HASSAN, SALES AND CONTRACTS IN EARLY ISLAMIC COMMERCIAL LAW (1997).

56. According to Islamic law, the Lawgiver, that is, God, has made a demand on human beings in five categories, thus, human conduct can be categorized into legal injunctions [*ahkam*] and assessed values by Islamic law. The five assessments are as follows: (1) *Wajib* or *Fard* [obligatory], (2) *Haram* [forbidden or prohibited],



classifications of *tasarruf* which do and do not lead to a contract, focus upon the volitive will to create or modify a right or responsibility.<sup>57</sup>

The Islamic legal definition of a contract places fundamental importance in the will or intent of each party. Some scholars define a contract as an agreement between two willing parties to establish, shift, or terminate a right.<sup>58</sup> Another way of looking at a contract under Islamic law is as “the connection of an offer with an acceptance in a lawful fashion, the effect of which occurs definitely upon the object of the agreement.”<sup>59</sup> A contract is thus formed at the time agreed upon by the parties by their mutual assent and not at the time it is memorialized in the form of a written agreement. A contract need not be written to be valid, although in certain cases, given the nature and subject matter of the contract, a written instrument may be required.

According to Islamic law, a contract must be externally expressed in words, via speech or otherwise. Writing is a mode of expressing the contract that, according to jurists, constitutes an admission [*iqrar*] of the fact that the contracting parties have *already* agreed. A contract, whether in writing or in other forms, requires the clear and precise expression [*jala al-ma'na*] of the will of both the offeror and the offeree.<sup>60</sup> Consequently, the written document itself neither creates nor modifies contractual rights or responsibilities, nor does it constitute the required offer and acceptance, but merely expresses such.

The majority of jurists have held that there are four<sup>61</sup> *arkan* (singular *ruk'n*), or required or necessary elements, to a sales

(3) *Mandub* [recommended], (4) *Makruh* [frowned upon or abominable], and (5) *Mubah* or *Halal* [permissible]. See generally AHMAD HASAN, PRINCIPLES OF ISLAMIC JURISPRUDENCE: THE COMMAND OF THE SHARI'AH AND JURIDICAL NORM (1993) (expounding upon these categories in greater detail).

57. See, e.g., Umar F. Moghul, *Contract Formation by Paper Clipping*, THE ISLAMIC BANKER, Oct. 2001.

58. In Arabic: *ittifaq iradatayn ala insha'i haqq aw ala naqlihi aw ala intiha'ih*.

59. In Arabic: *'irtibaat ijab bi qabul ala wajh mashru' yathbutu atharahu fi mahalihi'*.

60. To do so, it is often suggested that the past or present tense (rather than the future or imperative, for instance) be employed when contracting to ensure definitiveness and clarity.

61. Some jurists hold that there are three, combining the seller and buyer into a single *ruk'n*. See WAHBA AL-ZUHAYLI, FINANCIAL TRANSACTIONS IN ISLAMIC JURISPRUDENCE: A TRANSLATION OF VOL. 5 OF AL-FIQH AL-ISLAMI WA ADILLATUHU 8-9 (Mahmoud El-Gamal trans., 2003).

contract.<sup>62</sup> A *ruk'n* is that which is inherent or internal [*juz min haqiqah*] to the contract and which, if left absent or unfulfilled, renders the contract invalid such that all legal consequences of the contract (or action) do not follow.<sup>63</sup> For example, as generally accepted among jurists, the *arkan* of a sales contract are: "(1) a seller; (2) a buyer; (3) an object of the contract (both what is priced and the price itself); and (4) the expression of the contract (namely, manifestation of mutual assent in the form of offer and acceptance)."<sup>64</sup> In order to be valid and enforceable, a contract must first fulfill its *arkan*. For instance, if either an offer or acceptance is absent, the contract is invalid (meaning both *batil* and *fasid*, according to the majority position among the four Sunni schools of law, or merely *batil*, according to the Hanafis, one of the four Sunni schools of Islamic jurisprudence).<sup>65</sup>

A contract must, in addition, fulfill certain conditions [*shurut*, singular *shart*] to its validity. A *shart* is similar to a *ruk'n* in that it must be present for the contract to be valid. The similarity, however, ends there because unlike a *ruk'n*, a *shart* is external to [*kharij an haqiqah*] the contract.<sup>66</sup> Although jurists differ on the finer details, the conditions [*shurut*] to validity for a sales contract may be summarized as follows:

1. Adulthood, sanity and discernment of the contracting parties;<sup>67</sup>
2. Correlation between the offer and acceptance;<sup>68</sup>
3. Unity of contract session such that convention would not indicate a rejection of the offer;<sup>69</sup>
4. The object of sale is itself saleable property<sup>70</sup> and either

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62. *Id.* at 8-9. The following discussion of *arkan* and *shurut* is limited to *mu'amalat* and does not cover *'ibadat*.

63. ZAYDAN, *supra* note 49, at 59.

64. ZUHAYLI, *supra* note 61, at 8-9.

65. ZAYDAN, *supra* note 49, at 65-67.

66. *See id.* at 59.

67. Jurists typically require a person be adult, sane, and discerning to contract, but there are exceptions to this rule which lie outside the scope of this Article. Adulthood is generally defined as the onset of puberty, and discernment is the ability to competently handle one's financial affairs. *See* ZUHAYLI, *supra* note 61, at 351-58; ZAYDAN, *supra* note 49, at 91-144. *See also* KUTAIBA S. CHALEBY, FORENSIC PSYCHIATRY IN ISLAMIC JURISPRUDENCE 20-22, 37-53 (2001).

68. ZUHAYLI, *supra* note 61, at 19.

69. *See id.* at 19-26.

70. For a thing to be saleable, it must be lawful under the Shari'ah. Pork, for

- owned or in the possession of the seller and available and deliverable at the time of contract;<sup>71</sup>
5. The object of sale is known and sufficiently described;<sup>72</sup> and
  6. The price is specified and known at the time of contract.<sup>73</sup>

According to the majority position among the jurists of Islamic law, if any one of the above-listed *shurut* is absent or unfulfilled, the sale, act, or contract is invalid [*batil*].<sup>74</sup> However, Hanafi jurists opine that the absence of certain *shurut* render the contract *fasid*, meaning that certain but not all legal consequences may still follow from the contract.<sup>75</sup> Moreover, the missing *shart* can be supplied at any subsequent time. Once the *arkan* and *shurut* are all present for a particular transaction or contract, and if no legal impediments [*mawani*], such as coercion, are present, the contract, then, is valid [*sahih*].

## 2. *Riba*

Perhaps the most well-known principle of Islamic finance is the prohibition of *riba*, which in its most common contemporary understanding, is said to include interest on a loan.<sup>76</sup> Jurists have almost unanimously forbidden commercial bank interest.<sup>77</sup> One reason advanced for this is that the Shari'ah countenances lending money as a charitable activity and not necessarily a profit making venture. The prohibition of *riba* also applies to currency lending transactions and to trading that involves certain other commodities, such as certain foodstuffs, gold and sil-

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example, would not constitute a valid sale object for Muslims. See VOGEL & HAYES, *supra* note 4, at 94-95.

71. See ZUHAYLI, *supra* note 61, at 15-16; see also KAMALI, *supra* note 44, at 99-116 (2000) (discussing in detail the discourse regarding, and rationale underlying, these concerns).

72. See ZUHAYLI, *supra* note 61, at 36-48.

73. See *id.*

74. ZAYDAN, *supra* note 49, at 66.

75. See *id.*

76. Cf. ZUHAYLI, *supra* note 61, at 338. For an instructive essay on why not all interest constitutes the forbidden *riba* and why not all *riba* is interest, see Mahmoud A. El-Gamal, *An Economic Explication of the Prohibition of Riba in Classical Islamic Jurisprudence* (May 2, 2001), at <http://www.ruf.rice.edu/~elgamal/files/islamic.html>.

77. ZUHAYLI, *supra* note 61, at 339-52 (presenting and refuting the arguments of those who contend that banking interest should be permitted).

ver.<sup>78</sup> When these commodities are traded, the trades must be made in equal measure and without deferment.<sup>79</sup>

The prohibition against interest-based lending has not stopped contemporary Islamic finance from, in practice, formalistically finding ways around this prohibition. In practice, the economics of principal and interest have become couched in a contrived set of technical legal terms of art. This formalistic translation of interest-based lending into Islamic finance has not been accompanied by any practical effort that approaches, let alone overcomes, the substantive problems wrought thereby on the integrity of Islamic law and jurisprudence. It has caused interminable chaos *vis-à-vis* attempts to create an Islamic economy. The notion of prepayment serves as a specific example of the formalistic acceptance of practices that, arguably, are substantively forbidden by Islamic law.

Prepayments resulting in a reduction of the principal amount “owed” by “borrowers” are typically not allowed under Islamic law and Shari‘ah committees of most Islamic banks have chosen to abide, at least nominally, by this overt prohibition.<sup>80</sup> These same Shari‘ah committees have gone on to permit prepayments when they are couched in the language of “rebate” in spite of the fact that the end result is one and the same whether it is called a prepayment or a rebate.<sup>81</sup> In this and similar examples, the question that remains unaddressed is whether it is the form or substance of a prepayment which Islamic law views as problematic. The idea of an advance purchase, which is similar to the notion of a prepayment, has also been approved by certain Shari‘ah committees in the context of *murabahah*- and *musharakah*-based transactions.<sup>82</sup> It is, moreover, prohibited

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78. See IMRAN AHSAN KHAN NYAZEE, *THE CONCEPT OF RIBA AND ISLAMIC BANKING* 67 (1995). See also *id.* at 67-77 (discussing the *‘ilal* of *riba*). For a discussion of the extension of the prohibition of *riba* to modern currency, see *id.* at 79-93. See also ZUHAYLI, *supra* note 61, at 315-28. See generally IQBAL AHMAD KHAN SUHAIL, *WHAT IS RIBA?* (Rizwanullah & Zafarul-Islam Khan trans., Pharos Media & Publ’g Pvt. Ltd. 1999) (1936).

79. ZUHAYLI, *supra* note 61, at 311-14 (explaining the types of *riba*).

80. See USMANI, *supra* note 44, at 141-43. Those permitting as a general rule prepayments with a reduction in the debt owed rely on a *hadith* text the authority and authenticity of which is disputed. See *id.* at 142.

81. According to Zuhayli, “jurists agree that a debtor making a smaller prepayment in lieu of a larger debt that had not yet matured is permissible by ‘mutual consent’ [that takes place] *ex-post*.” ZUHAYLI, *supra* note 61, at 328.

82. Instances of both have occurred in the United States with certain Islamic home

under Islamic law for a borrower to be charged any late fees;<sup>83</sup> some contemporary jurists have, however, allowed late charges to the extent the lender argues it has actually incurred costs due to the payment being late.<sup>84</sup> Similarly, when a party defaults on its obligations, the defaulting party may be required to donate a specified amount to charity in lieu of paying penalties.<sup>85</sup>

As can be expected, there exist many other complexities and subtleties to the subject of *riba*, and those topics are beyond the scope of this Article. What is important to understand, though, is that the manifold rules of Islamic transactional law had traditionally been arrived at during premodern times through the methods of *usul al-fiqh* in such a way as to ensure that the fundamental principles prohibiting the practices of *riba* and *gharar*<sup>86</sup> were upheld. Now that conventional finance has made a norm of these practices, Islamic finance has in effect assumed them without analyzing their substantive validity, and is finding ways formalistically to integrate these erstwhile forbidden practices into the fold of Islamic law.

### 3. *Gharar*

Another key feature of Islamic finance is the prohibition of *gharar*, a term which has been translated as “trading in risk”<sup>87</sup> or “risk-taking”<sup>88</sup> and has been taken by jurists to refer to a lack of specificity in the terms of a financial contract. *Gharar* may be best understood as ignorance of the material attributes of a transaction, such as the availability or existence of the subject

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financing and refinancing structures. Interestingly, absent such a feature, the financing party may have run afoul of local usury laws. In such cases, Shari’ah committees have permitted the otherwise prohibited, under the laws of necessity, in order to comply with these local laws rather than using the rationale of alleviating the hardship (a purpose of Islamic law) that would result to homeowners absent such a prepayment feature.

83. See, e.g., QUR’AN 2:280 (stating “[a]nd if [the debtor] is in straitened circumstances, let there be postponement until [he is] in ease”).

84. USMANI, *supra* note 44, at 131-40. In representing various institutions, we have seen prepayments permitted in certain circumstances, such as home financing transactions.

85. *Id.* at 102.

86. See *infra* Part I.D.3.

87. See Mahmoud A. El-Gamal, *An Economic Explication of the Prohibition of Gharar in Classical Islamic Jurisprudence*, at 1 (May 2, 2001), at <http://www.ruf.rice.edu/~elgamal/files/islamic.html>.

88. See KAMALI, *supra* note 44, at 84 (suggesting that the “basic concern in all discussions of *gharar* is with elements of risk-taking”); see also *id.* at 84-98.

matter, its qualities, quantity, deliverability, and the amount, terms, and timing of payment.<sup>89</sup> For *gharar* to have legal consequences: (1) such *gharar* must be excessive and not trivial; (2) it must pertain to the subject matter of the sale; and (3) society must not be in need of the contract in question. This last requirement explains why forward sale [*salam*] and manufacture [*istisna'*] contracts have traditionally been permitted under Islamic law, despite the arguable presence of *gharar* in these contracts.<sup>90</sup> Broadly speaking, the taint of *gharar* can be prevented when the parties to a contract have adequate knowledge of the subject matter of the transaction and the counter-values they intend to exchange.<sup>91</sup> *Gharar* may also be limited and controlled through formal regulation.<sup>92</sup>

Jurists have debated the presence of *gharar* in those sales in which the object is not viewed before conclusion of the contract or in which the object is nonexistent at the time of entry into the contract.<sup>93</sup> Some jurists have held that the *gharar* in such cases is

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89. *See id.* at 84.

90. *Id.* at 85. *See e.g.*, ZUHAYLI, *supra* note 61, at 385 (citing Ibn Rushd debunking the position held by a small minority of Muslim jurists that prohibits leasing by arguing the sale object's existence is extremely likely); *see also id.* at 238 (stating "the forward sale [*salam*] contract was made an exception for the rule prohibiting the sale of non-existent items. This is a special license given to the people to meet their economic needs and facilitate their daily lives"); *see also id.* at 488 (stating the "permissibility of this contract [silent partnership or *mudarabah*] is viewed as an exception to general rules prohibiting excessive risk and uncertainty"); *see also id.* at 271 (stating that despite it being a non-existent item, *istisna'* [the contract of manufacture] is permissible by reasoning of *istihsan*, or equitable preference). For further information regarding *salam*, *see id.* at 237-66. For further information concerning *istisna'*, *see generally id.* at 267-80. For further information regarding *istihsan*, *see* ZAYDAN, *supra* note 49, at 230-35; ABU ZAHRAH, *supra* note 51, at 262-72; SOBHI MAHMASSANI, *FALSAFAT AL-TASHRI FI AL-ISLAM: THE PHILOSOPHY OF JURISPRUDENCE IN ISLAM* 85-87 (Farhat J. Ziadeh trans., 1961). *Istihsan* [equitable preference] is a proof in which a jurist gives preference to one of many possible solutions to a problem in order to comply with the objective of fairness in the Shari'ah. *Istihsan* differs from equity in Anglo-American law in that equity relies on the concept of natural law whereas *istihsan* relies on the ideas of fairness and conscience in the Shari'ah. Which of these solutions should be selected and why, as well as the degree of authority of *istihsan*, are among the considerations of *usul al-fiqh*. For a comparative analysis between *istihsan* and the doctrine of equity, *see* John Makdisi, *Legal Logic and Equity in Islamic Law*, 32 AM. J. COMP. L. 63, 66-85 (1985). Unlike the doctrine of equity in Western law, which "derives its legitimacy from the belief in a natural right or justice beyond positive law," *istihsan* is an integral aspect of Islamic law and it does not seek or recognize a law above and superior from it. *Id.* at 67.

91. *See* KAMALI, *supra* note 44, at 86.

92. *See id.* at 160-61.

93. *See id.* at 90-93.

excessive or exorbitant and others have held it to be minimal.<sup>94</sup> Many hold that in certain cases the absence of the object is outweighed by other, more important considerations. Examples of this abound in leasing [*ijarah*] and manufacturing orders [*istisna'*], in which the sale objects are nonexistent at the time of the contract, but are still permitted by jurists to be the objects of contracts because doing so is deemed to fulfill the needs of society.<sup>95</sup> As a result of the difference in opinion among jurists as to what constitutes the *'illah* of this ruling, some jurists have opined that the most important consideration in cases of nonexistent sale objects is not their existence but their deliverability.<sup>96</sup>

The notion of delivery is closely allied in Islamic law to the concept of possession [*qabd*], which a majority of jurists have held to be a requirement for a valid sale.<sup>97</sup> Jurists differ, however, on the definition of *qabd*. Many assert that it means actual, while others hold it to mean constructive, possession.<sup>98</sup> And still other jurists state that it is to be determined with reference to prevailing mercantile custom<sup>99</sup> since it is undefined in the textual sources and depends on the nature of the item.<sup>100</sup>

### E. *Precis of Murabahah*

#### 1. Definition of *Murabahah*

Sales are, generally speaking, classified as either *murabahah* or *musawamah*.<sup>101</sup> The primary distinction between the two arises from the requirement in *murabahah* that the seller inform the buyer of the seller's cost to obtain the item of sale and how much profit he will earn on the sale, whereas in the case of *musawamah*, no such disclosure is made.<sup>102</sup>

Often the term *murabahah* is translated as "cost plus mark-

94. *See id.* at 90.

95. *See id.* at 85.

96. *See id.* at 117-24 (citing a number of jurists from various Sunni schools of Islamic jurisprudence).

97. *See id.*

98. *See id.* at 121.

99. *Id.* at 121. Custom or habit, whether mercantile or otherwise, can be considered valid from the point of view of the Shari'ah if such a custom or habit does not contradict or contravene the Shari'ah. *See* NASR, *supra* note 9, at 121.

100. *See* KAMALI, *supra* note 44, at 120-21.

101. USMANI, *supra* note 44, at 96.

102. *See id.*

up sale.”<sup>103</sup> The Maliki school of Islamic jurisprudence defines the *murabahah* contract as one in which a “seller informs [a] buyer of the cost at which the seller obtained an object of sale [which is to be resold to such buyer] and collects a profit margin either as a lump sum, or the seller may state the profit margin as a percentage or ratio of the seller’s original purchase price.”<sup>104</sup> The Hanafis define it as the transfer of an object obtained through a prior contract in exchange for the original price plus a stated profit margin.<sup>105</sup> The Shafi’is and Hanbalis define it as the selling of a good at its original purchase price plus a profit, provided, in addition, that both parties know the original purchase price.<sup>106</sup>

Contemporary *murabahah* transactions may be described as follows: a person (the buyer) requests a party (the seller) to purchase an item so that the buyer can, in turn, purchase the same item from the seller. Presumably, the buyer cannot afford to pay in full on the spot and is unwilling to borrow conventionally. The seller informs the buyer of the price at which the seller will obtain or has obtained the item (the “Principal Cost”), and both parties agree upon a profit margin. Generally in contemporary Islamic financial transactions, the seller is a financial institution, and the sale by the seller to the buyer occurs on a deferred installment basis.<sup>107</sup>

Justice Taqi Usmani, who sits on the Shari’ah committees of many of the world’s largest Islamic financial institutions, has remarked that the manner in which *murabahah* transactions ought normatively to be implemented varies significantly from the manner in which Islamic finance implements them in the present day.<sup>108</sup> Modern Islamic financial institutions have taken this

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103. See *supra* note 15 (explaining further the term *murabahah*).

104. ZUHAYLI, *supra* note 61, at 353.

105. *Id.*

106. *Id.*

107. A valid deferred sale [*bay’ mu’ajjal*] does not entail *riba* (though it may involve interest) because the countervalues exchanged must be of a different class (e.g., an automobile and currency). The formal aspect of Islamic law does not dictate the economic criteria of how prices are to be determined. It should be noted that often Islamic banks use LIBOR or other similar references as benchmarks. See VOGEL & HAYES, *supra* note 4, at 139; cf. USMANI, *supra* note 44, at 119 (stating that “merely using the interest rate as a benchmark for determining the profit of *murabahah* does not render the transaction as invalid, *haram* or prohibited, because the deal itself does not contain interest. The rate of interest has been used only as an indicator or as a benchmark”).

108. See USMANI, *supra* note 44, at 104-05; see also VOGEL & HAYES, *supra* note 4, at



form of sale and modified it formalistically in ways that tend to blur the line as to its normative spirit. Despite this failing, the saving grace of contemporary Islamic financial practice is that the form, as commonly implemented today, is not without precedent in classical law and jurisprudence.<sup>109</sup>

## 2. Boundaries of Acceptability

Though the majority of jurists consider *murabahah* a permissible transaction, jurists of the Maliki school of Islamic jurisprudence find it relatively less desirable in comparison to other contracts of sale.<sup>110</sup> Jurists permitting such transactions cite the Qur'an as well as the rulings of other authorities.<sup>111</sup> According to Zuhayli, the *murabahah* "satisfies all the legal requirements for sale<sup>112</sup> and . . . provides a valuable service in economic markets."<sup>113</sup>

Present day jurists have divided contemporary *murabahah* transactions into two promises. The first is a promise by the seller to acquire an item, and the second is a promise by the buyer to buy from the seller the same item. Contemporary jurists in Islamic finance have chosen to rely on the minority Maliki position<sup>114</sup> that promises contained in the *murabahah* are

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140 (commenting "[m]urabaha[h] is now commonly in use only in a composite form" even though this form was known classically).

109. In a classical example, the scholar al-Shafi'i (d. 820) is quoted as having explained:

If an individual shows another a good and [referring to such good] says "Buy this, and I will give you this much profit," and then the second man buys it, then the purchase is valid. If the first man said, "I will give you this much profit, but I retain an option [to keep or return the good]," then he may conclude the sale or leave it.

ZUHAYLI, *supra* note 61, at 361.

110. See generally El-Gamal, *supra* note 76. It is unclear from El-Gamal's translation whether the Malikis simply find it less favorable or actually deem the transaction *makruh*.

111. Muslim scholars generally quote two verses of the Qur'an when discussing the legality of *murabahah*: "And God has permitted trade" (2:275) and "But let there be among you traffic and trade by mutual goodwill" (4:29). In buttressing the argument in favor of *murabahah* usage, jurists also cite a report from Ibn Mas'ud, a contemporary of the Prophet Muhammad, peace be upon him, stating the *murabahah's* permissibility. To understand the relevance that Islamic jurisprudence finds in such a report, see KAMALI, *supra* note 9, at 235-44.

112. See *supra* note 64 and accompanying text. See also *infra* Part I.E.3.

113. ZUHAYLI, *supra* note 61, at 354.

114. Observers of Islamic law may argue that in order to reach a desired legal outcome, these jurists have deviated from the opinions of their schools of jurispru-

binding [*lazim*] and not terminable at will, so long as the promisee has actually relied upon the promise.<sup>115</sup>

### 3. Conditions of Validity

As a sale, the *murabahah* contract must minimally fulfill the *arkan* and *shurut* normally associated with a sales contract.<sup>116</sup> The *murabahah* contract must also fulfill the following *shurut* particular to *murabahah* contracts:

1. The initial contract by which the seller purchases the good must be valid. If this initial sale is, for instance, defective or invalid, the subsequent sale to the buyer would not be permitted.<sup>117</sup>
2. The buyer must know the Principal Cost at which the seller obtained the item.<sup>118</sup>
3. The parties must have knowledge of, and specify at the time of contract, the profit margin because it is a component of the price at which the good is sold to the buyer.<sup>119</sup>
4. The Principal Cost for which the seller purchased the good must be fungible. If the Principal Cost is non-fungible, and the seller does not own the item, the sale would not be permitted since the object is not in the seller's possession and, therefore, its value is unknown. If the profit margin is made dependent on the Principal Cost (such as a percentage thereof), the sale would not be permitted because, again, the value of the non-fungible good is unknown.<sup>120</sup> If, however, the seller owns the item and pur-

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dence, thereby opening the door to methodological dissonance, among other things. Often the legal method of Shari'ah committees consists of a need to opine on a certain matter and to search for an opinion by any jurist no matter how obscure the opinion or the jurist. Rather than discover or derive law from the sources of Shari'ah, Shari'ah committees are often content, for various socio-historical reasons, to rely upon those existing rulings with which they are methodologically incompatible or, at worst, with which they personally disagree.

115. For his part, Zuhayli overcomes this criticism of methodological dissonance by asserting that the synthesis [*talfiq*] of the Hanafi and Maliki rulings is permissible because the two rulings pertain to two different issues. There is no harm, he contends, in following one jurist on one issue and another on another issue. This ruling also upholds "the stability of contractual obligations and [the] protection of the parties' economic interests." ZUHAYLI, *supra* note 61, at 361.

116. *See supra* Part I.D.1.

117. ZUHAYLI, *supra* note 61, at 361.

118. *See id.* at 355.

119. *See id.*

120. *See id.*

chased it by non-fungible means, the sale would be permitted so long as the profit margin has been clearly specified, is of another type of non-fungible good, and does not depend on the Principal Cost (such as a percentage thereof).<sup>121</sup>

5. When trading in goods, such as currency or certain foodstuffs, which are subject to the rules against *riba*, the validity of the *murabahah* requires that *riba* not have been present in the original sale. If *riba* inhered, then the purchased goods may not be sold via *murabahah* because the original sale would be itself invalid and the seller's profit in the subsequent sale to buyer would also constitute *riba* (or more specifically, *riba al-fadl*).<sup>122</sup>

To the foregoing list, contemporary jurists have attached additional *shurut*:

1. The seller must own the object<sup>123</sup> and bear the risks and responsibilities associated with ownership. The risks of loss and damage must be borne by the seller during such time as the good remains in his possession or ownership.<sup>124</sup> Though this may seem obvious, it is explicitly mentioned perhaps as a means of combating the loose manner in which some *murabahah* sales have been conducted.
2. The seller must have actual or constructive possession of the object of sale even if only for a short time.<sup>125</sup> It is quite likely that this is imposed because often in contemporary *murabahah* sales, the purchase by the seller occurs merely on paper, in which case he bears no true risk with regard to the good. It is also commonplace for ownership of the good to pass to the seller and immediately back to the buyer during the course of a single transaction closing. Shari'ah committees have come to accept this reality even though the infinitesimal holding period by the seller challenges the integrity of the first sale as independent of the second.
3. The good must have been purchased by the seller from a third party (i.e. a party other than the buyer). For the buyer to sell the item to the seller and then repurchase it

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121. *See id.*

122. *Id.*

123. *Id.*

124. USMANI, *supra* note 44, at 106.

125. *See id.*

from the seller is deemed a legal dodge or contrivance [*hila*, plural *hiyal*]<sup>126</sup> used to accomplish an otherwise forbidden interest-based [*ribawi*] financing.<sup>127</sup> Some jurists argue that even a three-party *murabahah* constitutes a legal contrivance,<sup>128</sup> though Shari'ah committees have generally allowed the buyer to act as agent of the seller.<sup>129</sup> In such cases, the two parties provide unilateral promises to one another to sell and buy the commodity.<sup>130</sup> The buyer purchases the good on the seller's behalf thereby acting as the trustee of the seller who is considered the actual owner and bearer of responsibility for the good.<sup>131</sup> The buyer then purchases the good from the seller.<sup>132</sup> Readers are reminded that these transfers of ownership between the parties actually take place simultaneously. Given the brevity of such ownership, whether the seller actually bears any risk with regard to the good while in the hands of the buyer is therefore arguable.

4. Contemporary jurists have permitted the buyer to provide security to the seller for his purchase. The only restriction imposed in this regard is that the security instrument (as well as the "promissory note," if any) be entered into only after ownership of the object of sale has transferred from the seller to the buyer, since the buyer only becomes indebted to the seller once the sale takes place.<sup>133</sup> It may be permissible, however, for the seller to take security from the buyer prior to the sale, provided

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126. SHERMAN A. JACKSON, ON THE BOUNDARIES OF THEOLOGICAL ACCEPTANCE IN ISLAM: ABU HAMID AL-GHAZALI'S FAYSAL AL-TAFRIQA BAYNA AL-ISLAM WA AL-ZANDAQA 88 (2002) (translating the Islamic legal term *hila* as "legal dodge").

127. *See id.*

128. SAEED, *supra* note 17, at 92-95.

129. *See* ZUHAYLI, *supra* note 61, at 627-89.

130. USMANI, *supra* note 44, at 106-08.

131. According to Professor Vogel, Islamic law does not hold liable a trustee [*amin*] unless he or she has negligently or intentionally damaged the item. *See* VOGEL & HAYES, *supra* note 4, at 112-14.

132. Shari'ah committees require that this sale take place through an offer by the buyer and an acceptance thereof by the seller, provided that the sale is not made a condition to the agency agreement or a condition to the purchase of the buyer as agent for the seller. In order to accomplish this requirement, Shari'ah committees are typically content so long as the sale takes place under a separate written instrument. While documenting each sale in separate written documents may be advisable, doing so would not create separate contractual agreements since the parties already have in mind the agency agreement or subsequent purchase when initially entering into the contract.

133. USMANI, *supra* note 44, at 109.

that the security remains the seller's responsibility.<sup>134</sup> Typically, the security instrument and/or "promissory note" are simply executed moments after the sale documentation is completed in the same closing. It is important to note that in instances of default, as mentioned previously, the price to be paid by the buyer cannot be increased. Instead, the buyer may be obligated to reimburse the seller for costs actually incurred as a result of the delinquent payment or to donate some amount to a charity.

5. Contemporary jurists have also permitted a guaranty. According to the classical ruling, no fee may be charged for providing this guaranty. Contemporary jurists, while citing this ruling, have begun to question its efficacy.<sup>135</sup> It is hoped that if the classical position is reversed, it will come about not by what has become, among Shari'ah committees, the usual reference to the "rule of necessity" — an oblique way of deriving law — but by a more fundamental analysis that looks to the *'ilal* and *hikam* — and thereby to the substance — of the original rulings.

#### 4. Determination of Price

Jurists agree on the importance of disclosing the amount of the purchase price and its components. They differ, however as to the constituents of the purchase price. Ibn Rushd, a classical jurist of the Maliki school of jurisprudence, organizes into three categories what may be factored into the price: (1) that which can be included by the seller as part of its Principal Cost and which may be factored into the calculation of the profit; (2) that which can be included by the seller as part of its Principal Cost but not factored into the calculation of profit; and (3) that which cannot be included as part of the seller's Principal Cost nor used in the calculation of profit.<sup>136</sup>

For the Maliki school of jurisprudence, expenses of the first category are those relating to the essence of the goods [*ta'thir fi ayn*], such as dying or tailoring a piece of material which is to be sold.<sup>137</sup> In other words, all costs customarily associated with the

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134. *Id.* at 127.

135. *Id.* at 129-31.

136. 2 IBN RUSHD, *THE DISTINGUISHED JURIST'S PRIMER: A TRANSLATION OF BIDAYAT AL-MUJTAHID* 256 (Imran Ahsan Khan Nyazee trans., 1996).

137. NABIL A. SALEH & AHMAD AJAJ, *UNLAWFUL GAIN AND LEGITIMATE PROFIT IN*

object of sale and which result in an increase in its value may be appended to the Principal Cost. Expenses of the second category do not affect the essence of the good and are those incurred for services that the seller requires but cannot itself provide, such as transportation or storage. Expenses of the third category are those that do not affect the essence of the good and which are incurred for services the seller himself is able to provide, such as commissions or wages to its employees.<sup>138</sup>

The Hanbali school of jurisprudence holds that all actual expenses incurred by the seller may be added to the Principal Cost provided that the buyer is made aware of the nature and amount of such expenses.<sup>139</sup> The Shafi'i school rules similarly.<sup>140</sup> For the Hanafi school, all amounts normally accepted by commercial practice and actually incurred by the seller may be added to the Principal Cost.<sup>141</sup>

It should also be noted that the seller must make certain disclosures with regard to the amounts constituting and characteristics of the price.<sup>142</sup>

## 5. Right of Rescission

In certain instances, the contract may be unmade or undone from the beginning. According to the majority ruling, in the event of a mistake with regard to the amount or the characteristics of the purchase price (such as whether the seller purchased on a deferred basis) and a defect in the good, the buyer is granted the option either to return the object and be refunded the total purchase price, or to receive a price reduction

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ISLAMIC LAW: RIBA, GHARAR, AND ISLAMIC BANKING 118 (Graham & Trotman 1992) (1986).

138. See IBN RUSHD, *supra* note 136, at 347. See also SALEH & AJAJ, *supra* note 137, at 118.

139. SALEH & AJAJ, *supra* note 137, at 118.

140. *Id.* at 118-19.

141. ZUHAYLI, *supra* note 61, at 357.

142. For instance, if the seller initially purchased the object on a deferred basis, he must disclose this fact to the buyer. *Id.* (stating that "[t]his follows since deferment normally results in an increase over the cash-and-carry price"). The jurist al-Shafi'i opines that the buyer is to be given a deferral period mirroring that of the seller. See *id.* If the seller purchased the object in exchange for a debt, he need not disclose this fact to the buyer. Only the price (i.e., the amount of debt) needs be disclosed. If the seller purchased the object as compensation for an unpaid loan, it may not be resold using *murabahah* with the price as the original loan amount. See *id.*

and retain the object.<sup>143</sup> The Hanbali school asserts that the sale remains binding in the event the price is erroneous, but its price must be corrected.<sup>144</sup> The Shafi'i school holds that the price is to be corrected and the profit accordingly reduced.<sup>145</sup> There are many more rulings in this regard, and to enumerate them all would fall outside the scope of this Article.

## 6. Contemporary Criticisms

Common criticisms of contemporary *murabahah* transactions stem from the function and role of the seller and the practical implementation of the transactions. Finance on the basis of profit and loss sharing, with which the theoretical model of Islamic banking is identified substantively, does not seem to be a dominant characteristic of modern *murabahah* sales. Of course, the criticism that contemporary *murabahah* does not comport with the original spirit of Islam is a criticism that can just as easily be directed toward the entire practice of contemporary Islamic finance. The very substance of a *murabahah* dictates, among other things, that the seller be exposed to the risks normally associated with ownership, such as the risk of loss, damage, and deterioration of the goods prior to delivery. The seller must also accept the buyer's ability to return the good and rescind the sale if the goods are damaged, deficient, do not meet the buyer's preferences, or involve a mistake in pricing.

In engaging in *murabahah* transactions as sellers, Islamic banks do not share in the profits and losses of their customers, rather they assume the role typical of conventional banks. In some cases, the risks normally associated with ownership are transferred contractually to the buyer. In other instances, the seller does in fact bear such risks from the time of purchase until the time of delivery, leading some to argue that the bank takes a risk, which justifies the profit, until the client fulfills his original promise to purchase the commodity.<sup>146</sup> The counterargument is that the seller does not *really* own the good, never truly has physical or even constructive possession of the good, and owns the item for only moments, as both sales are concluded at the same

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143. *Id.* at 357-58.

144. IBN RUSHD, *supra* note 136, at 258.

145. *Id.*

146. *See* SAEED, *supra* note 17, at 85-87.

closing. Effectively, the seller-bank does not bear the risks of ownership.

Rights of the customer-buyer, such as the right to inspect the goods and the right to rescind the sale, are typically nullified or shifted so they become beneficial to the seller rather than to the buyer. Some classical jurists held that such reallocations could take place if buyers were to affirmatively waive their rights. Affirmative waivers do not occur as often as constructive waivers in contemporary Islamic finance.

Moreover, according to many *murabahah* contracts, the buyer is responsible for compliance with all applicable laws and regulations, including those relating to the import of goods.<sup>147</sup> In short, the seller-bank has now effectively avoided many, if not all, of the risks and responsibilities that classical jurisprudence expects it to bear.

The risk that the buyer may refuse to buy is avoided by means of an advance payment, “promissory note” security, third-party guaranty, and/or contract terms, such as those mentioned previously.<sup>148</sup> Some Islamic financial institutions use these measures well in advance of purchasing the item and deposit assets and collateral to be held until they have been fully paid. Typically, for example, the advance payment amount would be sufficient to cover any loss that may occur from a refusal by the buyer. Alternatively, the seller-bank may contractually be afforded the right, if the customer-buyer refuses delivery, “to sell the goods at the prevailing price in the market . . . [and if such sale price is insufficient] to demand from the client the balance [of what is due to the Bank, including the profit margin].”<sup>149</sup> Perhaps the factors discussed above led the Council of Islamic

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147. *Id.* at 92. For example, a *murabahah* contract of Faisal Islamic Bank of Egypt states:

The client is responsible for all other expenses, which are not included in the cost structure of this [*Murabaha*] [sic] contract, and also for all costs arising from cancellation of a documentary credit, or refusal of the exporter to supply the goods. The client does not have any right to demand from the Bank any compensation in case the exporter refuses to supply the goods for any reason whatsoever.

*Id.*

148. Providing security or giving a guaranty for a debt are not in itself reprehensible or prohibited under Islamic law, but there are specific rules for each.

149. SAEED, *supra* note 17, at 86 (quoting the *murabahah* contract of the Faisal Islamic Bank of Egypt).



Ideology to comment that in *murabahah* transactions, there is “the possibility of some profit for the banks without the risk of having to share in the possible losses, except in the case of bankruptcy or default on the part of the buyer.”<sup>150</sup> It is argued, thus, that contemporary *murabahah* provides the bank with a predetermined return on capital.<sup>151</sup>

As mentioned previously, penalties and fees for late payments were prohibited traditionally but are now allowed in a somewhat conspicuous fashion as part of most modern Islamic financial transactions. Some contemporary jurists have observed that the penalty imposed is actually calculated by means of a bank doing nothing more than examining its normal rates of return. This is not dissimilar to conventional banks’ seeking to recover the opportunity cost of their capital.<sup>152</sup>

In cases of other Islamic financial institutions, the penalty does differ from those found in conventional banking. In our experience, we have seen penalties equal to specified amounts that have no relation to the amount of indebtedness. We have also seen penalties equaling a percentage of the delinquent payment amounts and charged once per delinquent payment without recurrence or compounding. In other instances, we observed institutions charge a percentage of the delinquent amount and agree contractually to deduct their expenses from this amount and to donate the excess to charity.

150. *Id.* at 87.

151. *See id.* at 95. Predetermined profit on the investment of money is typically deemed to be an unlawful gain, which is prohibited under Islamic law. *See e.g.*, USMANI, *supra* note 44, at 50. Rather, an investor must share in the profits and losses, if any, in a business venture or underlying physical asset. Profit sharing ratios may be specified, but profit itself may not be assured. *See id.*

152. The Faisal Islamic Bank of Egypt’s standard *murabahah* contract states: Since the bank does not deal with interest, any delay in paying the installments when they are due as agreed upon causes serious harm to the bank, which requires compensation. This is on the basis of the [S]hari’a[h] rule that no harm should be inflicted on any party [to the contract], which is the basis of transactions. . . . [T]he two parties agree that in case of delay by the second party in paying any installment on its due date, the bank has a right, without any objection or dispute [by the client], to demand compensation for any damages occurred because of the delay. The value of this damage will be calculated on the basis of average realised profit for the period in addition to any other compensations. Any dispute in relation to whether [Faisal Islamic Bank of Egypt] deserves compensation or not, or the value of such compensation will be decided by the [religious supervisory board of the Islamic bank].

SAEED, *supra* note 17, at 90-91.

Forecasting the abuse of *murabahah* transactions discussed above, as well as those present in the case of *Symphony Gems*, discussed in Part II *infra*, Justice Taqi Usmani writes:

It should never be overlooked that, originally, *murabahah* is not a mode of financing. It is only a device to escape from “interest” and not an ideal instrument for carrying out the real economic objectives of Islam. Therefore, this instrument should be used as a transitory step taken in the process of the Islamization of the economy, and its use should be restricted only to those cases where *mudarabah*<sup>153</sup> and *musharakah*<sup>154</sup> [a partnership] are not practicable.<sup>155</sup>

What the foregoing illustrations and our own experience impress upon and instill in us is the realization that increasing instances of superficial overlap between Islamic financial practices and conventional practices — based on formalistic adherence to Islamic law — are coming at an immense expense to the spirit and wisdom of the Shari‘ah. The facts and outcome of *Symphony Gems* constitute the latest indication of the rising irrelevance of Islamic jurisprudence to Islamic finance, as this is a case in which an ostensibly Islamic contract (a *murabahah*) made by an Islamic financial institution by its own terms invoked the coverage of a non-Islamic legal system and the jurisdiction of a non-Muslim court. No contemporary jurist ought to overlook the onslaught being inflicted upon the integrity of Islamic law as the essential aspects of the Shari‘ah — those which, for instance, allow jurists to argue that one mode of transaction is categorically better than another — are altogether being driven out of Islamic finance, in large part because contemporary jurists have failed to recognize that arriving at a formal concordance between Islamic finance and conventional finance need not and should not mean setting aside an active utilization of the tools and techniques of Islamic jurisprudence when Islamic jurisprudence itself comprises the only gateway Islamic finance may avail itself of to reach Shari‘ah compliance.

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153. *Mudarabah* is a contract whereby a party entrusts another party with the investment and management of its money or other assets. For further detail, see ZUHAYLI, *supra* note 61, at 483-515; SAEED, *supra* note 17, at 51-59, 69-75; SALEH & AJAJ, *supra* note 137, at 126-43.

154. For an explanation of *musharakah*, see ZUHAYLI, *supra* note 61, at 445-82; SALEH & AJAJ, *supra* note 137, at 113-17; SAEED, *supra* note 17, at 59-75.

155. USMANI, *supra* note 44, at 104-05.

II. ISLAMIC INV. CO. OF THE GULF (BAHAMAS) LTD. V.  
SYMPHONY GEMS N.V. & OTHERSA. *U.K. Court Construing Islamic Law*

*Islamic Investment Company of the Gulf (Bahamas) Ltd. v. Symphony Gems N.V. & Others*<sup>156</sup> (“*Symphony Gems*”) is a watershed decision not only because it is the first case concerning the construction of an Islamic financial transaction to be brought before a U.K. court.<sup>157</sup> The case is also of great value because it highlights some of the most pressing challenges facing the development and refinement of Islamic finance as a contemporary practice. One significant challenge is the question of how actors on both sides of the Islamic-conventional divide ought to go about integrating Islamic finance into the scheme of conventional finance. Heard before the High Court of Justice Queen’s Bench Division Commercial Court, and decided on February 13, 2002, by Justice Tomlinson, *Symphony Gems* centers on a financing facility based on the previously discussed *murabahah* contract as set forth by the transacting parties in a “*Morabaha* [sic] Financing Agreement.”

B. *The Contractual Dispute in Symphony Gems*

In January 2000, the claimant Islamic Investment Company of the Gulf (Bahamas) Ltd. (“IICG”) entered into a *murabahah* financing agreement (the “Contract”) with the defendant Symphony Gems N.V. (“Symphony”). The Contract envisaged that IICG would provide a revolving purchase and sale facility to enable Symphony to purchase certain inventory, namely precious stones and gems. The Contract, according to the terms contained in its recitals, intended for the financing to follow the form of a *murabahah* transaction and, thereby, to be in compliance with the Shari’ah.

The Contract clearly identified the structure of the purported *murabahah* transaction whereby Symphony, as buyer, would identify precious gems or stones that IICG, as seller, would purchase and immediately resell to Symphony at an agreed-upon profit margin. The Contract made further refer-

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156. 2002 WL 346969 (Q.B. Com. Ct. Feb. 13, 2002).

157. As of yet, no commercial case involving Islamic finance has appeared in a U.S. court.

ence to a purchase contract (the "Purchase Contract"), an agreement whereby IICG would purchase the gems from a supplier and sell the same to Symphony. If and when Symphony ever sought to use the financing facility, it was to issue an irrevocable offer to IICG identifying the gems to be financed, as well as the supplier of such gems and other relevant contractual details including the date of payment by IICG to the supplier (the "Settlement Date"). This offering document could be accepted by IICG no later than the second business day preceding the Settlement Date. If accepted, a Purchase Contract would have been formed that, among other things, contained a definition of the "Cost Price" (the price payable by IICG to the supplier of the gems) and a definition of the "Sale Price," (the price payable by Symphony to IICG in installment payments). The difference between the Cost Price and the Sale Price included an agreed-upon margin that would correspond to IICG's profit on the transaction.

Before the Contract could be made to take effect, however, a number of other documents were required to be executed as conditions precedent, including a

form of offer, form of acceptance, form of personal guarantee, form of bank guarantee, form of deed of pledge, form of collection agreement, form of assignment of receivables agreement, form of market rate agreement and form of letter from Beautiful Diamond Ltd . . . [and] three legal counsels' opinions, two from Belgian legal counsel and one from Swiss legal counsel.<sup>158</sup>

The Contract specified details relating to the passage of title and various conditions precedent which Symphony was required to satisfy before utilizing the financing facility. When IICG engaged in a purchase under the Contract, IICG was to forward payment to the account of the supplier designated by Symphony, which in turn was "absolutely, unconditionally and irrevocably"<sup>159</sup> obligated to purchase the gems from IICG. In fact, Symphony was obliged to inform the gem supplier that upon passage of title to IICG, such title would immediately thereafter pass to Symphony. Pursuant to the Contract's terms, Symphony accepted personal responsibility for selecting each proposed sup-

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158. *Islamic Inv. Co. of the Gulf (Bahamas) Ltd.*, 2002 WL at \*5-6.

159. *Id.* at \*2.

plier of the gems and for payment to the supplier regardless of any “defect, deficiency or any loss or any breach”<sup>160</sup> of the sale between the supplier and IICG. Symphony was further obligated to pay IICG for the full amount of the gems regardless of whether title or the goods themselves had passed to IICG or Symphony. The seller was in no way liable contractually for the condition or quantity of the goods and their compliance with whatever expectations or arrangements Symphony might have with the gem supplier. According to the Contract, risk relating to the goods was to be borne by IICG for so long as IICG bore title to such goods, though IICG expressly disclaimed any liability for the goods while in transit. According to its own terms, the Contract was to be governed by, and construed in accordance with, English law and was subject to the exclusive jurisdiction of the English court. Lastly, it should be noted, the obligations of Symphony under the Contract were guaranteed by two personal guarantors.

The Court notes that it consulted with two experts in the area of Islamic law and has been briefed on the nature of *murabahah* contracts. One such expert, Dr. Yahya al-Samaan, is quoted by the court as explaining the contemporary *murabahah* to be “a transaction intended to assist a person who seeks to purchase goods of a certain description but who is unable to pay for the goods in cash.”<sup>161</sup> He continued, “As viewed by Islamic jurists, the *Morabaha* [sic] contract was originally a contract in respect of a commodity available in the market. However, Islamic banks have given the *Morabaha* [sic] contract a wider interpretation that includes the importation by the relevant bank of specified goods from abroad.”<sup>162</sup> The court comments that although the Contract is *prima facie* governed by English law (because it states so and there is no reason to refute the parties’ preference), “it is equally critical to note that that Dr. Samaan, after examining the nature and terms of the [C]ontract comes to the conclusion that . . . the [Contract] does not have the es-

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160. *Id.*

161. *Id.* at \*4.

162. *Id.* Dr. al-Samaan is said also to have gone on to describe what this Article has explained as to the mechanics of *murabahah* sales, *supra* Part I.E, detailing the two promises made by the contracting parties, the requirement of actual possession by the seller-bank, and its liability during such possession.

sential characteristics of a *Morabahah* [sic] contract.”<sup>163</sup> No doubt Dr. Samaan’s denial that the Contract is a *murabahah* sale provides additional — though unnecessary — support for the court’s finding that the Contract must be construed “according to its terms as an English law contract.”<sup>164</sup>

### C. *Facts and Posture of Symphony Gems*

In February 2000, Symphony identified a company named Precious Ltd. (“Precious”), located in Hong Kong, which was to supply a very large quantity of rough diamonds. Symphony noted these facts in its two offers to IICG sent on February 10th and 21st. These offers stated Settlement Dates of February 14th and 25th, respectively, and IICG accepted these offers on the 12th and 24th of February, respectively. IICG then proceeded to make payment in full to the account of Precious, although no payment had yet been made by Symphony.

During the period preceding litigation, the defendants (Symphony and its two guarantors) posited that Precious was a reputable diamond broker and that it had paid amounts to obtain certain rough diamonds to a sight holder, which in turn failed to honor its commitment to Precious. The failure came as the result of an ongoing family dispute between one of the guarantors of Symphony and his two brothers who controlled the company to which Precious had made payment to acquire the goods under the Contract. Extensive correspondence primarily between Symphony and Precious followed. Correspondence from the defendants to IICG, however, did not contend that their failure to pay came as a consequence of their not having received the goods.

When Symphony did not repay IICG in full, IICG enforced the security it had been granted and sought to reclaim the balance of unpaid amounts by instituting proceedings for summary judgment on the basis of nonpayment. Symphony responded by asserting non-delivery of the goods. The court rejected this defense relying on “proper construction of the [Contract],”<sup>165</sup> citing several sections of the Contract in which delivery was not mentioned as a prerequisite to payment by Symphony.

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163. *Islamic Inv. Co. of the Gulf (Bahamas) Ltd.*, 2002 WL at \*4-5.

164. *Id.* at \*5.

165. *Id.* at \*8.

Symphony also contended that since the Contract was in reality a purchase and sale agreement, IICG's claim to recover the Sale Price should fail because there had been no delivery to Symphony. In response to this argument, the court held that the absence of delivery could arise only if Symphony had failed to make the necessary arrangements.

Symphony's argument that the Contract violated the principle of illegality was also rejected. Symphony claimed that because some part of the transaction took place under the laws of the Kingdom of Saudi Arabia where the Contract would be prohibited, the principle of illegality should be applied to render the Contract unenforceable. The court held, however, that that portion of the transaction occurring or having a nexus to Saudi Arabia was so minor that the principle of illegality could not successfully be invoked.

Lastly, the defendants put forth an argument of *ultra vires*. The court assumed, without deciding, that the Contract would be deemed invalid as a *murabahah* and would therefore be inconsistent with IICG's charter, which demands compliance with Islamic law in all its dealings. Analyzing the *ultra vires* law of the Bahamas, where IICG is chartered, the court found that IICG was not subject to the *ultra vires* doctrine. Accordingly, even if the Contract may have been shown to be beyond the scope of its objects, it could not have been set aside or avoided on the grounds that it was void *ab initio*.

Symphony's attempt to avoid paying liquidated damages — to do so would be contrary to Islamic law according to many contemporary jurists — was rejected by the court on the grounds that the claim was brought under English law by a Bahamas company, and not a Saudi Arabia company. The law of the Bahamas as passed through the English court does not prohibit the payment of *riba*.

#### D. Analysis of Symphony Gems

##### 1. Was the Contract a Valid *Murabahah*?

As already noted by Dr. Al-Samaan at trial, the Contract fell short as a *murabahah* sale because the required *shurut* were not present. In this sense the Contract is, based on our experiences, fairly representative of many, if not most, purported *murabahah* transactions in contemporary Islamic finance. Specifically, the

contracting parties ignored the requirements that IICG own and/or possess the goods for sale.<sup>166</sup> The supplier, in this case Precious, was simply to send the goods directly to the buyer, thereby bypassing the seller. The various risks of ownership typically borne by the seller in a valid *murabahah* were avoided by having title immediately transfer to Symphony and by contractually shifting several responsibilities normally borne by the seller to the buyer.<sup>167</sup> Other Islamic legal rights were discarded, such as that of Symphony to reject the goods if certain defects were found to be present.<sup>168</sup> The notion that Symphony was responsible for payment to IICG regardless of delivery is a notion that obviously parallels an obligation to repay indebtedness more closely than it parallels how payments are typically made in a spot sale. Though it is possible that Symphony waived its Islamic legal rights and chose to bear these responsibilities itself, it seems more likely, given the circumstances of this case and the superior bargaining posture inherent to commercial banks, that IICG sought to mimic conventional interest-bearing financing to the greatest extent possible by imposing these provisions upon its customer Symphony.

Even if the Contract were to constitute a valid *murabahah* sale, conventional finance would consider its structure and procedures a curious and awkward deviation from the most efficient and optimal course of business. Moreover, since the parties deviated from the Shari'ah *anyway* — an argument that can be made, we posit, against most contemporary versions of Islamic contracts — the transaction seems even more awkward, if not ludicrous. Given the manner in which typical *murabahah* sales (and most Islamic financial transactions) are carried out today, we wonder about the extent to which the jurists who sit on Shari'ah committees at Islamic financial institutions actually meditate on the wisdom their legal reasoning is supposed to contain rather than rely mainly on the formal aspects of what they approve, based on mere appearance, as Shari'ah-compliant.

## 2. Governing Law

Parties to Islamic finance transactions often assert English

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166. See *supra* note 71 and accompanying text.

167. See *supra* notes 123-35 and accompanying text.

168. See *supra* note 143 and accompanying text.



or New York law as the governing law relying on the probability that the contracts are more likely to be enforced as written. *Symphony Gems* certainly bolsters the case for such reliance. Both Symphony and IICG sought to benefit by choosing, *ab initio*, a jurisdiction and a law which they expected would enforce the Contract as written, rather than reframing it, if necessary, as a true — or truer — *murabahah* sale. Perhaps they knew, or at least should have known since they had a Shari'ah committee advising them, that their transaction was blatantly problematic from an Islamic legal perspective. Nonetheless, at trial Symphony still nominally invoked the Shari'ah in an effort to defend itself and minimize its financial liability.

If a hypothetical Islamic court had jurisdiction over the dispute, it could have overlooked the invocation of English law and enforced the transaction based on the parties' intent to transact Islamically, just the same way the English court overlooked the Islamic legal form to enforce the transaction pursuant to English law. If the hypothetical Islamic court had construed the transaction as a *murabahah* sale, it would have applied the *fiqh* (akin in many respects to regulations) relating to *murabahah* sales. It would have found the transaction to be *batil* or *fasid*, depending on the school of jurisprudence applied. This ruling might very well have resulted in an outcome more favorable to Symphony. One cannot predict, however, whether the hypothetical court would have gone so far as to find the transaction to be abusive, or even a legal contrivance [*hila*]. Nor can one predict whether the hypothetical court would have sought to undo the deal altogether or even to reprimand the parties.

### 3. Documenting the Agreement

As mutually unfamiliar first principles and legal concepts mingle, contemporary Islamic finance and the transactions composing it can be a challenging, if not an essentially impossible, activity. First and foremost, the transaction must be documented in a manner agreed upon by the parties with their various Shari'ah committees and understandings of Islamic law. Documentation must comply with applicable local law, and, to the extent possible, Islamic law. Of course, where there is a conflict between Islamic and local laws, local law must prevail. As noted earlier, to ensure compliance with Islamic law, Shari'ah committees often seek out and rely on tenuous opinions with

which they as jurists may even intellectually disagree and which barely pass muster under the rubric of Islamic jurisprudence. In other instances, transactional lawyers resort to oblique drafting techniques and the use of legal contrivances to please the transacting parties and their Shari'ah advisors.

External pressures, especially those arising out of the desire for favorable tax treatment, are known to influence the way Islamic financial transactions are documented. As perhaps can be expected, parties prefer favorable tax treatment, such as having the ability to deduct interest payments from taxable income, although this may, in many, but not necessarily all cases, result in less substantive adherence to the Shari'ah. For their part, tax regulators may need to see in the transaction certain structural elements as well as certain key legal expressions before granting favorable treatment. In contrast, Shari'ah committees, instead of concerning themselves with what is meant by the conventional legal expression, seem to prefer to altogether forego examination of tax issues and tax documentation. In our experience, Shari'ah committees do not always concern themselves with the tax (and, to a lesser extent, accounting) treatment of Islamic financial transactions, contending that such treatment *per se* does not render such transactions impermissible from an Islamic point of view. Nevertheless, the tension of arguing to one party, such as the retail public, that an instrument is not interest-bearing,<sup>169</sup> while asserting to tax regulators that it is, poses serious ethical concerns for jurists and leads to incoherent rulings and internal dissonance.<sup>170</sup> Those factors also highlight the lack of

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169. Muslims conversant in English do not usually appreciate the technical difference between the Islamic legal term "*riba*" and the conventional finance term "interest" and often use the terms interchangeably as if they were direct translations of one another (which they are not).

170. The notion that Islamic law is itself unpredictable and unstable is often erroneously stated by many and the incoherence evident among juristic rulings relating to Islamic finance serves only to exacerbate this existing problem. Federal law has made reference to Islamic lawmaking using the term *qadi* (the Arabic term for a judge or justice and sometimes spelled *kadi* or *cadi*) to indicate a system of arbitrary lawmaking. See e.g., *Terminiello v. Chicago*, 337 U.S. 1, 11 (1949) (commenting "[w]e do not sit like a *kadi* under a tree dispensing justice according to considerations of individual expediency"); *United States v. Murray*, 621 F.2d 1163, 1169 (1st Cir. 1980) (analogizing unreasoned and "unprincipled" administrative rulings to "decisions of *Kadi* at the gate"); *Colonial Trust v. Goggin*, 230 F.2d 634, 636 (9th Cir. 1955) (commenting that this court cannot apply "such abstract theory of justice which might be entertained by an oriental *cadi*"); *Clark v. Harleysville Mut. Casualty Co.*, 123 F.2d 499, 502 (1941) (stating "[w]e sit, after all, as an appellate court, administering justice under the law, not as an

any intellectual discourse whatsoever among contemporary jurists regarding the direct transferability between Islamic legal and conventional legal regimes of basic concepts and definitions. It is highly problematic that contemporary Islamic jurists tend to assume without arguing that any given English or U.S. technical legal term such as, *inter alia*, “sale,” “loan,” or “property,” magically satisfies the Islamic legal definition for such word’s non-technical Arabic correspondent.

### CONCLUSION

As societies constantly change, the legal particulars [*fiqh*] of Islam as they pertain to financial transactions also must modulate and adapt if application of the Shari‘ah is to remain relevant to contemporary human life and thought, lest they become drowned out by the cacophony and internal dissonance created by stagnant and intellectually bereft scholarship. In the face of such necessity, we propose that the Islamic financial complex, together with the broader faculty of contemporary jurists and *mujtahids* worldwide, set forth to build, or rebuild, a complete Islamic financial-legal system utilizing *as a bridge*, but *not as a foundation* the terminology and ideas of the modern financial system which are today in ascendancy. This proposed Islamic financial-legal system would not be merely a high-handed imitation of conventional financial norms reliant on the very letter and spirit of the modern system it is meant to displace. Rather, it would be an organic continuation of classical Islamic financial understandings and practices, unlike the translated mimicry which constitutes contemporary Islamic finance.

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ancient oriental *cadi*, dispensing a rough and ready equity according to the dictates of his own unfettered discretion”). Legal scholars have refuted this stereotype. See e.g., Makdisi, *supra* note 88, at 63-66.

For a thorough and enlightening discussion of judicial process, adjudication and judicial discretion, as well as the notion of precedent generally, see MOHAMMED FADEL, *ADJUDICATION IN THE MALIKI MADHHAB: A STUDY OF LEGAL PROCESS IN MEDIEVAL ISLAMIC LAW* (1995). The role of principles in the development and exposition of the law is demonstrated briefly but well by Mohammad Hashim Kamali, *Qawa'id al-Fiqh: The Legal Maxims of Islamic Law*, at <http://www.aml.org.uk/journal/>. For a discussion of the relationship between Islamic law and the Common Law, see John A. Makdisi, *The Islamic Origins of the Common Law*, 77 N.C. L. REV. 1635 (1999). While it may be true that Islamic law as used today — in contrast with the classical or medieval periods — in the practice of contemporary Islamic finance and banking has made Islamic law seem unpredictable and unstable, to blame solely Islamic law and its jurists of yesterday and today would be a shallow understanding of the matter.

There is no reason why lawyers and financiers today cannot be loyal to the content of classical Islamic financial law, as well as to the intellectual and metaphysical spirit that gave rise to it, without necessarily having to duplicate its various forms. As *Symphony Gems* demonstrates, the attempt merely to manipulate form at the expense of spiritual substance can be, at worst, an exercise in either folly or futility, or both. At best, its results can be no more than formally sufficient, yet substantively bereft. With a firm foundation in the roots and substance of the Shari'ah, particularly the science of *usul al-fiqh* which is all too often ignored in the present day, Islamic jurists and *mujtahids* together with lawyers and financiers can work towards building a contemporary Islamic financial system according to the Islamic religion, but through concepts derived from the English language and current in Anglo-American law, since English is now the most universal language of thought and Anglo-American law the most universal model of governance.

By using Anglo-American legal concepts as a starting point rather than an ending point, while focusing on the substance and purposes of the Shari'ah, the result would be that a lawyer or financier involved in Islamic finance need not try, on the one hand, to build an Islamic financial complex based on conventional economic principles, and, on the other hand, to think in an Arabic manner while simultaneously reading and writing in English. This balancing act can be undertaken if jurists and *mujtahids* meet four criteria. First, they should develop a universal set of financial-legal maxims, representing the distilled essence of Islamic law, which would serve to inform and guide professionals undertaking Islamic finance. Second, they should cultivate an appreciation for, if not comprehension of, the Islamic wisdom tradition.<sup>171</sup> Third, they should return to using the pow-

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171. See WILLIAM C. CHITTICK, *THE HEART OF ISLAMIC PHILOSOPHY: THE QUEST FOR SELF-KNOWLEDGE IN THE TEACHINGS OF AFDAL AL-DIN KASHANI* 66 (2001). The Islamic wisdom tradition sets the goal of knowing oneself in terms of the Absolute Being that brought the universe into existence, and of acting in accordance with what this knowledge demands. Thus, Islamic wisdom, and any discipline seen through its lens,

can only understand human beings in terms of the unity of the human world and the natural world. There is no place in this tradition to drive a wedge between humans and the cosmos. In the final analysis the natural world is the externalization of the human substance, and the human soul is the internalization of the realm of nature. Human beings and the whole universe are intimately intertwined, facing each other like two mirrors. The quest for wisdom

erful science of *usul al-fiqh* in place of the uncritical and unwise reliance on *fiqh* which pervades Islamic finance today. Fourth, they should facilitate and participate proactively in the development of a financial technology native to the soil of Islamic thought. We cannot overemphasize the need for concentration and vigilance to ensure that any transfer or continuation of knowledge based on the foregoing criteria maintains transparency with regard to both the form and substance of Islamic law, which the Anglo-American outcome is meant to render *vis-à-vis* the original Arabic outcome.

As long as this new expression of traditional Islamic financial law in the Anglo-American context remains true to its roots in Islamic wisdom, its intrinsic economic justice would be universal. No person operating within this paradigm need necessarily be Muslim to take advantage of its ultimate insistence on economic justice rather than only wealth enhancement. Yet, until this new expression of Islamic financial law is developed and refined, Western courts will find themselves, as they continue to rule on Islamic financial transactions, invoking an Islamic law with faulty precedents such as *Symphony Gems*, where contemporary Islamic finance has made itself look, at best, incoherent, and at worst, irrelevant.

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can only succeed if the natural world is recognized as equivalent to one's own self, just as one must see the whole human race as the external manifestation of the potencies and possibilities of the human soul.