

Make Yourself



Shariah-Compliant



Overview

- Importance of Sharī'ah Compliance in mu'āmalāt
- Understanding the basic requirements for Sharī'ah Compliance
- Addressing common financial and legal issues facing a UK resident Muslim
- Summary / Acknowledging our duty as Muslims



Sharī'ah defined

- Lexically – 'a way to the watering place'
- Occurs only once in the Holy Qur'an in contradistinction with hawā' – whimsical desire:

ثُمَّ جَعَلْنَاكَ عَلَىٰ شَرِيعةٍ مِّنَ الْأَمْرِ فَاتَّبِعْهَا وَلَا تَتَّبِعْ أَهْوَاءَ الَّذِينَ لَا يَعْلَمُونَ (١٨) [الجاثية]

Thus we put you on the right way [Sharī'atin] of religion. So follow it and follow not the whimsical desire (hawā') of those who have no knowledge.

[45:18]

- Used commonly to refer to commands, prohibitions, guidance and principles that Allah swt has addressed to mankind pertaining to conduct in this world and salvation in the next.
- Basic purpose – to enable man to forsake the dictates of hawā'; to lead him to righteousness and truth; to make him upright and worthy of the divine trust of the vicegerency of Allah swt on earth.



Importance of Sharī'ah Compliance in mu'āmalāt

- A Muslim is one who submits in all walks of life

يَا أَيُّهَا الَّذِينَ آمَنُوا ادْخُلُوا فِي السَّلْمِ كَافَّةً وَلَا تَتَّبِعُوا خُطُواتِ الشَّيْطَانِ إِنَّهُ لَكُمْ عَدُوٌّ مُبِينٌ (٢٠٨)
[البقرة]

O you who believe! Enter into Islam in totality, and follow not the footsteps of the Satan for he is to you an avowed enemy. [2:208]

- Two types of devotional acts - 'ibādāt
 - by essential nature – Salāh, Zakāt, fast, Ḥajj, 'Umrah, dhikr, Qur'ānic recitation, etc
 - by virtue of adherence to the Qur'ān and Sunnah – all civil transactions

عَنْ عَبْدِ اللَّهِ قَالَ قَالَ رَسُولُ اللَّهِ صَلَّى اللَّهُ عَلَيْهِ وَسَلَّمَ: « طَلَبُ كَسْبِ الْحَلَالِ فَرِيضَةٌ بَعْدَ الْفَرِيضَةِ ». [البيهقي]

It is reported by Ibn Mas'ūd, he said: The Messenger of Allah sws said: To search for Ḥalāl earning is an obligation after the obligation. [Baihaqī]



- Even temporal and mundane practices acquire a sacred moral character when they conform to Divine prescriptions.

عَنْ سَلْمَانَ قَالَ: قِيلَ لَهُ: قَدْ عَلَّمَكُمْ نَبِيُّكُمْ صَلَّى اللَّهُ عَلَيْهِ وَسَلَّمَ كُلَّ شَيْءٍ حَتَّى الْخِرَاءَةَ. قَالَ: فَقَالَ: أَجَلٌ لَقَدْ نَهَانَا أَنْ نَسْتَقْبَلَ الْقِبْلَةَ لِغَائِطٍ أَوْ بَوْلٍ أَوْ أَنْ نَسْتَنْجِيَ بِالْيَمِينِ أَوْ أَنْ نَسْتَنْجِيَ بِأَقْلٍ مِنْ ثَلَاثَةِ أَحْجَارٍ أَوْ أَنْ نَسْتَنْجِيَ بِرَجِيعٍ أَوْ بِعَظْمٍ. رواه مسلم [كتاب الطهارة، باب في الاستطابة]

It is reported from Salmān that it was said to him: Your Apostle sws teaches you about everything, even about excrement. He replied: Yes, he has forbidden us that we should face the Qiblah at the time of excretion or urination, and that we should cleanse with the right hand or with less than three pebbles, or with dung or bone.

[Muslim]

- Civil transactions arguably form $\frac{3}{4}$ of Sharī'ah injunctions
 - 3 of the 4 volumes of The Hedāyah pertain to mu'āmalāt



- Acceptance of even purely devotional observances - 'ibādāt depends on correct observance of the rules on mu'āmalāt:

عَنْ أَبِي هُرَيْرَةَ قَالَ قَالَ رَسُولُ اللَّهِ صَلَّى اللَّهُ عَلَيْهِ وَسَلَّمَ « أَيُّهَا النَّاسُ إِنَّ اللَّهَ طَيِّبٌ لَا يَقْبَلُ إِلَّا طَيِّبًا وَإِنَّ اللَّهَ أَمَرَ الْمُؤْمِنِينَ بِمَا أَمَرَ بِهِ الْمُرْسَلِينَ فَقَالَ (يَا أَيُّهَا الرُّسُلُ كُلُوا مِنَ الطَّيِّبَاتِ وَاعْمَلُوا صَالِحًا إِنِّي بِمَا تَعْمَلُونَ عَلِيمٌ) وَقَالَ (يَا أَيُّهَا الَّذِينَ آمَنُوا كُلُوا مِنَ طَيِّبَاتِ مَا رَزَقْنَاكُمْ) ». ثُمَّ ذَكَرَ الرَّجُلَ يُطِيلُ السَّفَرَ أَشْعَثَ أَغْبَرَ يَمُدُّ يَدَيْهِ إِلَى السَّمَاءِ يَا رَبِّ يَا رَبِّ وَمَطْعَمُهُ حَرَامٌ وَمَشْرَبُهُ حَرَامٌ وَمَلْبَسُهُ حَرَامٌ وَغَدَى بِالْحَرَامِ فَأَنَّى يُسْتَجَابُ لِذَلِكَ ». [مسلم]

Abū Huraira reported Allāh's Messenger sws as saying: O people, Allāh is Good and He therefore accepts only that which is good. And Allāh commanded the believers as He commanded the Messengers by saying: “O Messengers, eat of the good things, and do good deeds; verily I am aware of what you do”. And He said: “O those who believe, eat of the good things that We gave you”. He then made a mention of a person who travels widely, his hair dishevelled and covered with dust. He lifts his hand towards the sky (and thus makes the supplication): “O Lord, O Lord,” whereas his diet is unlawful, his drink is unlawful, and his clothes are unlawful and his nourishment is unlawful. How can then his supplication be accepted?

[Muslim]



- Shortfall in purely devotional observances can be made up by qada', bequest for fidyah and repentance
- Transgressions in civil rights cannot be made up except by forgiveness by the one to whom the rights are due
- Economic activity is merely a means to the ultimate goal of establishing justice, fulfilling Allāh's will, achieving felicity of the Hereafter

وَابْتَغِ فِيمَا آتَاكَ اللَّهُ الدَّارَ الْآخِرَةَ وَلَا تَنْسَ نَصِيبَكَ مِنَ الدُّنْيَا وَأَحْسِنْ كَمَا أَحْسَنَ اللَّهُ إِلَيْكَ وَلَا تَبْغِ الْفُسَادَ فِي
الْأَرْضِ إِنَّ اللَّهَ لَا يُحِبُّ الْمُفْسِدِينَ [القصص]

And seek with the wealth Allāh has bestowed upon you the other world. And do not forget your portion in this world. But do you good, as Allāh has done good to you. And seek not occasions for mischief in the land, for Allāh loves not those who do mischief. [28:77]

- Wealth should be utilised to further the interests of the Hereafter



Basic requirements for Sharī'ah Compliance

- The subject matter of any transaction must be Sharī'ah-compliant
 - Transacting in unlawful commodities or investing in an interest-based bank is not compliant
- The transaction must not involve any interest based lending or borrowing
 - 33% maximum toleration in otherwise compliant shares?
- The transaction must not involve gharar – uncertainty or hazard caused by lack of clarity regarding the subject matter or its counter-value
- The documentation/contract wording must conform to Sharī'ah principles



Basic requirements for Shari'ah Compliance

4 key areas in contemporary contracts

Contemporary contracts fall foul of Shari'ah Principles in **FOUR** key areas:

- I. Seller not having ownership/possession of goods or selling something that is not in existence yet – e.g. financial markets such as derivatives and options and short selling
- II. Contracts must be devoid of excessive uncertainty (gharar)
- III. Penalty clauses which require the householder to pay interest charges if they default on payment
- IV. Mutually inconsistent contracts must not be made contingent on one another – e.g. hire purchase agreements



Conventional Mortgage Alternatives (Ribā-Free Home Purchase Plans)

- Why are conventional mortgages not permitted?
- How do 'Islamic' Home Purchase Plans differ?

Murābahah

- Customer promises the bank to purchase the identified property from the bank
- Customer promises the bank to purchase the identified property from the bank
- Bank purchases property from vendor e.g. £100,000
- Customer purchases the property from bank for £150,000 payable in instalments over a period e.g. 10 years
- Title is transferred to customer at time of sale but is mortgaged to secure customer's instalment payments
- Home insurance is usually required and is payable by the customer as owner
- Early settlement requires payment of full price unlike conventional mortgages – but bank may unilaterally waive some instalments

key challenges

- Legal enforceability of promise



Ijārah wa Iqtinā‘

- Customer enters into a promise to lease agreement with the bank for the property identified by the customer
- Bank purchases property from the vendor e.g. £100,000
- Bank leases the property to the customer for an agreed period
 - Customer pays rent + an on-account payment held in trust by the bank
- At the end of the lease period bank sells the property to the customer for £100,000 from the on-account payments

Key challenges

- Legal enforceability of promise
- Bank use of on-account payment
- Rental being linked to LIBOR
- In 2006 HSBC ceased this type of home purchase plan in the UK



Diminishing mushārahah

- Customer promises the bank to purchase the identified property from the bank
- Joint ownership – *shirkat-ul-milk* is created in the desired property: usually c. 70% financier - 30% client
- Separate unilateral promise from client to purchase financier's undivided share (حصة مشاعة) in units.
- Bank's share is leased to the client by a separate contract
- Customer pays rent + an on-account payment held in trust by the bank
- Actual periodic purchase of units of the financier's undivided share by exchange of offer and acceptance – preferably at market price, but can also be at the price promised by the client.
- Adjustment of the rental to reflect the decreased ownership of the financier.



Key challenges

- Shirkat-ul-milk or shirkat-al-‘aqd
 - Shirkat-ul-milk – neither party intends to make a profit on the property so advance agreement of price for sale of share is not prohibited
 - Shirkat-ul-‘aqd – bank only engages to make a profit so price of share cannot be fixed in advance
- Legal enforceability of promise
- Rental being linked to LIBOR

Anvantages of DM

- Bank can utilise on-account payment after purchase of share by customer
- Ownership of property transfers to customer sooner than the Ijārah plan



Conventional Bank Accounts

- Why are [most] conventional bank accounts not permitted?
 - **Basic bank account**
 - No cheque and no overdraft facility – use of only available funds
 - **Current Account**
 - Cheque book and overdraft facility
 - May give a low interest return
 - **Savings Account**
 - Deposit Account – higher rate of interest than CA
 - Cash ISA – higher return than DA + no tax on the interest with a limit of £5,100 per tax year
 - Fixed Notice (60/90 days etc) – withdrawal penalty if without notice
 - etc – generally the longer the withdrawal term the higher the return
 - **Free** overdraft facility?



Ribā-Free Bank Accounts

- How do 'Islamic' bank accounts differ?
- Current Account
 - Chequebook and multi-functional bank card
 - Loan by client to bank?
 - Money becomes property of bank
 - Bank has corresponding liability to customer
 - Payment by A to B by cheque (£100) is transfer of debt
 - i.e., A's bank now owes B £100 instead of owing to A



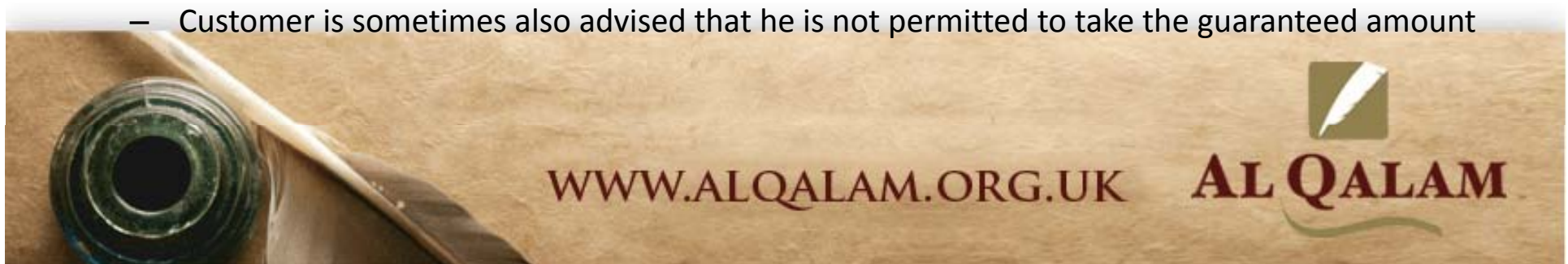
Ribā-Free Bank Accounts

- Current Account
 - Deposit by client at the bank?
 - Bank is safe keeper only
 - Money is available for immediate withdrawal
 - Bank cannot use money without consent
 - Payment by A to B by cheque (£100) is transfer of money, not debt – i.e., A's bank now holds £100 for safe keeping on behalf of B
 - If bank utilises the deposit with permission it becomes a deposit of guarantee
 - No modern bank has sufficient funds to guarantee all deposits so any such guarantee is worthless
 - If it is now considered a loan then it is this sale of debt (بيع الدين) or transfer of debt - ḥawālah?



Ribā-Free Bank Accounts

- Savings Account – muḍārabah/wakālah
 - On Demand Savings Account– based on Muḍārabah
 - Fixed Term Deposit Account (3, 6, 12, 18, 24 months) – based on Wakālah
 - 60 Day Notice Account - based on Wakālah
 - Restricted – requires bank to invest in only certain kinds of assets on both Sharī'ah and commercial grounds
 - Unrestricted – bank can invest in any Sharī'ah-compliant manner
- Recorded as assets of the bank when in fact the bank is a muḍārib/wakīl
- Profit equalisation reserve (PER) must be from share of muḍārib/wakīl
- Bank can advertise expected yield based on past performance and contribution from PER
- **SOME KEY CHALLENGES:**
- All commercial banking organisations in UK are subject to regulations on capital certainty
 - Creates a problem as profit & loss must be shared
 - IBB has attempted to resolve this by a 'voluntary gift' from the PER – amounts to a capital guarantee
 - Customer is sometimes also advised that he is not permitted to take the guaranteed amount



Conventional Bank Cards

- **Debit Card**
 - Linked to bank account
 - Solo/Electron – availability of funds is checked
 - Switch/Visa/Delta - availability of funds is not checked, may have over draft facility, may exceed overdraft
 - Less interest than Credit Card
- **Charge Card**
 - Creates a debt with often no spending limit payable in full by due date or otherwise incurs severe late fees
- **Credit Card**
 - Creates a debt with minimum payable and balance carried forward as interest bearing loan



Use of Conventional Bank Cards

- **Debit Card**

- Permissible - as long as the cardholder does not exceed the available balance in his account and no interest charge arises out of the transaction. [AAOIFI Standards, p. 21]
- Based on a restricted ḥawālah (الحوالة المقيدة) contract wherein the bank (المحال عليه) is already indebted to the cardholder (المحيل)

- **Charge Card**

- Not permissible unless the cardholder is not obliged to pay interest in the form of late fees?
- Based on an unrestricted ḥawālah (الحوالة المطلقة) contract wherein the card issuer (المحال عليه) is not already indebted to the cardholder (المحيل)



Use of Conventional Bank Cards

- **Credit Card**

- Not permissible by consensus if interest is paid
- If interest is not paid:
 - Not permissible – permissibility is not dependent solely on the result of the contract but also on the form which here includes an agreement to pay interest
 - Permissible – interest condition is void whilst the loan is valid as a loan is initially a gratuitous contract even if the loan is returned at the end
 - Valid but not permissible as although the interest condition is void and the contract valid, agreeing to the interest condition is a sin
- Based on an unrestricted ḥawālah (الحوالة المطلقة) contract wherein the card issuer (المحال عليه) is not already indebted to the cardholder (المحيل)



Islāmic Credit Card

- Current structures of 'Islāmic' credit cards are not 'credit' cards in the conventional sense but rather debit cards
- A South East Asian solution – based on bey' al-īnah
 - Customer purchases an asset from bank on deferred basis at price P
 - Bank buys back the asset at spot at price P-1
 - Price P-1 is deposited in to a Wadī'ah Account from which the customer makes purchases or cash withdrawals
 - Bank may also allow customer to use funds in excess of the balance of the Wadī'ah Account on the basis of qarḍ ḥasan
- Critics of the bey' al-īnah construct argue that it is ethically flimsy as the sale transacted is a fake sale and thus just a means of masking ribā.



Islāmic Credit Card

- A GCC solution – based on tawarruq
 - Bank purchases an asset from the market at cost C and sells it to the customer on a deferred basis at $C+1$
 - Customer sells the asset in the market to a third party in a spot sale at C
 - C is deposited in to a Wadī‘ah Account from which the customer makes purchases or cash withdrawals
 - At the end of every month, the value of total transactions by the customer is computed. A fresh tawarruq for this value is undertaken to replenish the Wadī‘ah Account.



Prepaid Mastercard

- **Cordoba Gold Cashplus Prepaid Mastercard**
 - UK's first prepaid Shariah compliant Mastercard card launched 11/08/2008
 - No interest charges, late payment fees or minimum monthly payments
 - User purchases the card from Cordoba Financial Group (est. 2006) for a small fee (£9.95) which covers administration costs
 - Cardholder tops up card at a top-up point and the value is deposited in an escrow account with AFL Bank [an SPV] within 24 hours as a trust.
 - A monthly fee (£4.95) is levied if there is a balance on the card
 - Whilst physical isolation of the funds of each individual account is not possible, it is entered on the banks balance sheet as an amount due to a specific individual [and not as a loan] and is not used by the bank nor entered as an asset of the bank
 - Purchases/withdrawals + transaction fee are deducted from the escrow account and the balance on the account cannot be exceeded



Personal Loans

- What is **WRONG** with a conventional personal loan?
 - What about Student Loans?
 - Can loans be linked to the consumer [or other] price index and thus interest paid at the rate of inflation?
 - Return of same units of measure \neq same value of the loan
- <http://www.alqalam.org.uk/UserFiles/File/StudentLoans.pdf>
- How does an 'Islamic' 'loan' work?
 - Commodity Murābahah
 - What is Tawarruq (monetization) and how does it work?

SOME KEY CHALLENGES:

- Why is it controversial? Is there an alternative?
- Also need to consider if the underlying need for the loan is valid



Tawarruq

- ‘Tawarruq’ is derived from *الْوَرِق* - minted silver coins
- ‘Tawarruq’ is not found in Arabic lexicons, only *الإيراق* – to have abundant wealth and *الاستيراق* – to seek *الْوَرِق*
- ‘Tawarruq’ is coined by [Ḥanball] Fuqahā’ *لمن يتكلف الحصول على الورق*
- Tawarruq = ‘to purchase a commodity on credit and then sell at spot to a third party at a loss with the objective of acquiring cash’
- The dominant opinion of Imām Aḥmad and the math-hab of the school – permitted
 - According Ibn Teymiyyah and Ibn al-Qayyim – *makrūh*
- The Shāfi‘ī School – permitted as they also allow *bey’ al-‘īnah*
- The Mālikī School – permitted but do not allow *bey’ al-‘īnah*
- Ḥanafī School – most have considered tawarruq and *bey’ al-‘īnah* to be the same
 - According to Imām Muḥammad – *makrūh*
 - According to Imām Abū Yūsuf – permitted
- Ibn al-Humām has reconciled the two (which many Ḥanafī fuqahā’ have also adopted) by attributing the above two opinions to *bey’ al-‘īnah* and tawarruq respectively. However, the latter is *khilāf al-awlā*.



Tawarruq

- Customer requires £10,000 for 12 months
- Customer promises to purchase a commodity [copper] from the bank on deferred payment basis over 12 months
- Customer appoints bank's employee as his agent through a restricted Power of Attorney to purchase the commodity on his behalf
- Bank sells commodity to customer [through his Attorney/bank employee] at cost plus profit [12.5%] payable over 12 months
- After possession, customer sells the commodity through a previously appointed third party broker
- Payment [£10,000] credited to the customer's account
- Customer makes monthly payments [£1,250] to the bank



Car & Equipment Leases

- Are conventional leases Sharī'ah-compliant?
- Responsibilities of lessor & lessee
- Penalties on default
- Mutually contingent contracts in hire-purchase

KEY CHALLENGE:

- Live within our means?
- Tolerated if lessee is sure he will not default on payments?



Guarantees, Warranties & Breakdown Cover

- Are guarantees permitted?
- Are extended warranties considered to be insurance?

<http://www.alqalam.org.uk/UserFiles/File/guarantee%20and%20extended%20warranty%20fatwa.pdf>

- Is Breakdown Cover permitted?

Some key challenges:

- What is the difference between a guarantee, a warranty and insurance?
- Is breakdown cover insurance, a guarantee or a warranty?



Insurance & Takaful

- So what's **WRONG** with conventional insurance?
- So how does 'Islamic' insurance work?
 - Takaful?
- What about those scholars who view conventional insurance as permitted?

SOME KEY CHALLENGES:

- How to resolve key issue of Gharar?
- 'Aqd Tabarru'and debate around this



Key outcomes of this session are to:

- Raise awareness of some of the key legal / financial areas where Muslims need to be aware of Sharī'ah principles to either avoid what is clearly unlawful or to fulfill an obligation
- To suggest ways for further study as this session is simply to raise awareness and each area needs more research
- Most importantly for you, the audience to recognise that disseminating and implementing this knowledge amongst the community is a personal challenge!



Any Questions ?

