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The Shari'ah Scholar's Journal

And when it is said to them: «Create not disorder on the earth», they say: «We are only promoters of peace».
Surat Al-Baqarah, 2:12 Holy Quran

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Editorial

Dear Readers

Islam is the religion of nature, a complete way of life. Its teachings are a guarantee for the success of mankind in this world and hereafter. The teachings and principles of Islam are so complete and compact, for every walk of life from faith and worship up to moral character and behaviour that by adopting and following them, one not only gets assured of benefits of Akhirah (the life hereafter), his life becomes peaceful, happy and satiating in this world too. As a matter of fact the complete and consummate teachings of Islam vis-à-vis finance and economy would definitely lead to social equality and a sound economic balance. Furthermore, the needs and necessities of people belonging to each and every social strata gets fulfilled in a just and fair manner.

Islam has given clear guidance about uplifting the poor and needy sections and individuals of the society, fulfilling their basic needs. Implementing and acting upon such teachings at individual and collective levels would certainly provide support to poor and the downtrodden sections. They can become self-dependent. Moreover, not only their economic condition improves, rather academic and mental level also develop considerably.

The Waqf has a paramount role to play in the economic set-up of Islam. The significance of Waqf has been retold in a number of Ahadeeth and traditions. It has been greatly emphasized and declared as a Sadaqat-ul- Jariyah (Continuous Charity). Since time immemorial, the Islamic Awqaf has played a vital role in fulfilling the needs and necessities of the poor and the needy, making them financially self-dependent, imparting education to Muslims, serving the sick and the disabled and financially aiding the men of letters, in the perspective of Islamic history throughout every era. The well-endowed, wealthy Muslims have been instrumental in establishing small and big Awqaf for the purpose of different religious, academic, social and welfare objectives, throughout the epochs of time.

In this perspective, emphasis should be laid upon making the Muslims inclined towards establishing new Awqaf besides safeguarding the existing ones. In fact, efforts should be made to spur such inclinations so that the tradition of Waqf (which holds enormous benefits not only for the Muslim society but the entire mankind), continue to be promoted.

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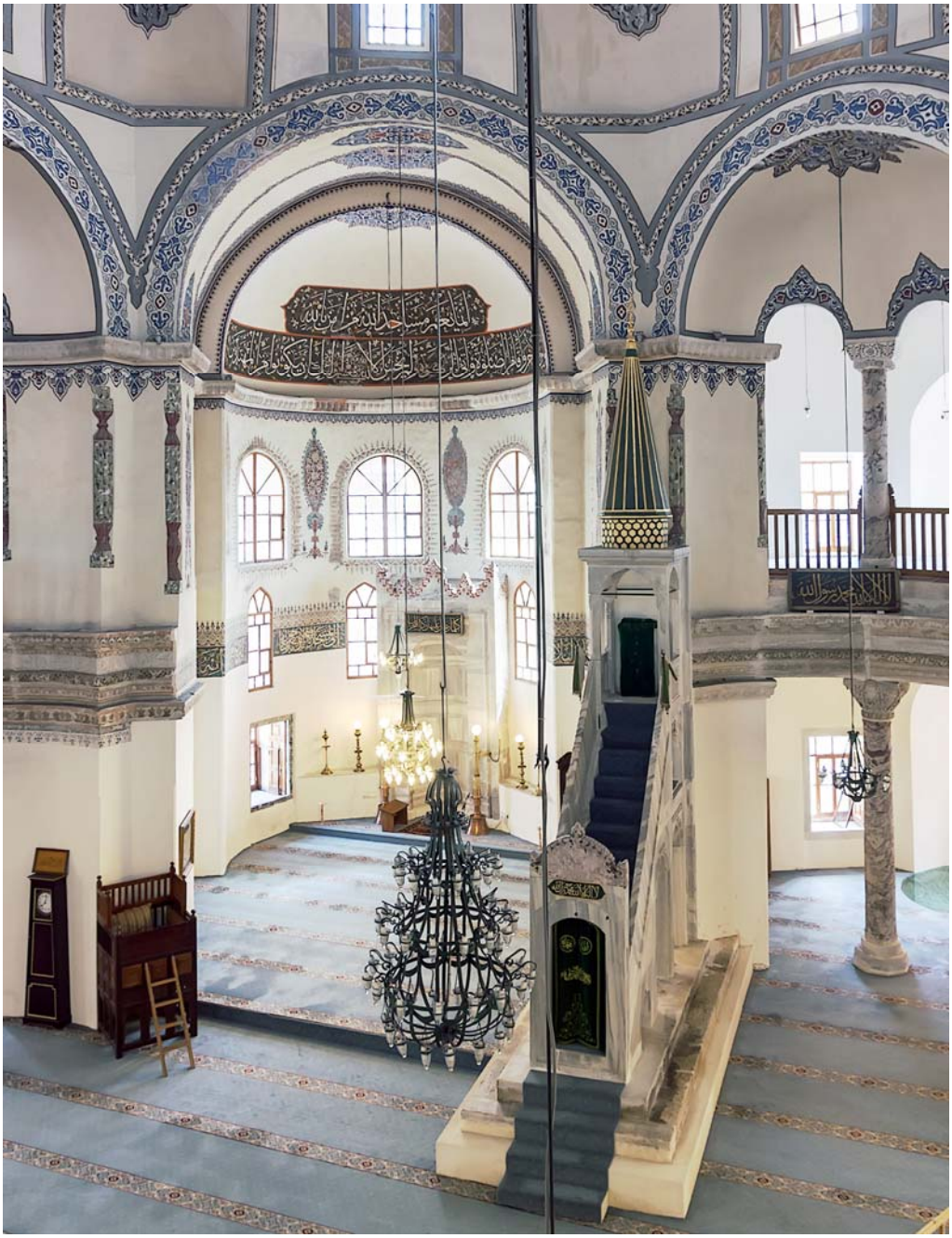

contents

Islamic Banking

By Sheikh Dr. Mohammed Ali Elgari

How an Islamic bank work, differences and similarities with conventional banking and major modes of finance. Financial inter-mediation is considered as a basic necessity for every human society in the past and today . History books have always noted the persistent determination of ancient communities for adopting specific arrangement which satisfy their financial inter-mediation requirements Creation of money (which liberated production resources and safeguarded means of saving methods) has caused division between individuals, namely the surplus category, which owns financial resources over their immediate needs. The deficit category which require financial resources more than they actually have. Human societies have recognized the need for adopting certain arrangements that will enable the transfer of the surplus to the category of deficit which will virtually entail more economical growth and development as well as high standards of welfare and prosperity for all people.

By the birth of the specialization era and division of work, many profitable activities have changed into institution with specific functions. The same thing can be said about the financial inter-mediation that had been practiced within the framework of social relationship, when monks working at their monasteries, Pharaoh, tribal *sheikhs* and senior traders etc, undertook the role of financial inter-mediation.

However, things had evolved to specialized institutions conducting financial inter-mediation, namely the banks. Traditional banks had therefore been set up to offer financial inter-mediation through loan (from surplus category) and lending (to deficit category). Conditional profit in loans evolved in order to cover the expenses and achieve profits to depositors. Banks in the beginning were maintaining deposits free of charge.

When fierce competition surfaced between banks, they were unable to attract savings without stipulating terms of profits to the depositors. Therefore, traditional bank became a loan seeking and lending institution whose underlying source of income is the difference between positive and negative interest. But, was it possible for the depositors to give loans directly to the investors without the services of the bank?

Contemporary analysis look at the bank as specialized information institution. Securing of true information, follow up and collection of data are indeed a highly expensive processes, yet such banks apart from individual are enjoying the characteristic of economies of large scale which enables such banks to pursue the above processes in a relatively low expenses.

Therefore the conventional work of the bank had been based on isolation of

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depositors (surplus category) from investors and those seeking finance for their projects (deficit category), as depositors normally do not give attention to the risks of end lenders, as they only take the risk of depositing their monies at the bank, if there is any.

However, the bank takes the risk of end lenders whom it had separated from sources of money. Though, if the lender fails to cover payment of its debts, then the risk will be borne by the bank itself and in normal cases should be indemnified from its profit or capital. However, observers to development of banks in recent days, see clear debility of the role of commercial banks which are based on the concepts of loan giving and lending in sophisticated economies, mainly because improvements relating to maintaining the information and methods of surveillance have led creditors to lean directly towards contacting the investors. Money markets have therefore played an increasing role in financial inter-mediation because they give the creditors the opportunity of bearing direct risks on behalf of the users of money, while the function of banking institution is management on behalf of others, maintaining service charge and arrangement of deals … etc, are seen by many observers as a trend which will prevail for long time over the contemporary financial development and will lead, as time passes to a further deterioration in the traditional role of the commercial bank (i.e. isolation of risks).

We would see for example, that the revenues acquired by banks such as service charge are increasingly growing in relation to revenue from profit. For the purpose of illustration, the share of commercial banks decreased in the last twenty years in the total U.S financial assets from 40% to 25%, because they were directed towards management of monies instead of lending. As a result of this different mode, securitization were widely spread, giving the depositors the chance of bearing the responsibility of direct risk of money.

Islamic bank is best known for its financial inter-mediation function which operates without interest. Since about one century ago, *Muslims* had reached the conclusion that the interest given by banks is the core of forbidden usury, because the increase in the loan which is the fundamental function of traditional banks is considered as part of usury and for this reasons banks were not widely known between *Muslims* except during colonial periods – despite its long rooted practice by the Europeans, since many hundreds years go. *Muslims* had therefore strived, after maintaining independence by their respective countries to establish banking systems that will be harmoniously coherent with the rules of *Shari'ah* (Islamic law).

They realized that financial inter-mediation is deemed to have been a basic function in the life of human societies and that *Muslims,* had adopted long time ago certain arrangement which would fulfill the need of financial inter-mediation. Transfer of money from the surplus category (i.e. the number of individuals and institutions that owned financial resources surpassing their immediate demand) to the deficit category (i.e. those who require financial resources over-exceeding what they now acquired) were conducted in the past in accordance with the *Mudaraba* mode.

Taqi Usmani

Mufti Muhammad Taqi Usmani is one of the leading Islamic scholars living today. He is an expert in the fields of Islamic Jurisprudence, Economics, Hadith and Tasawwuf. Born in Deoband in 1362H(1943 CE), he graduated par excellence form Dars e Nizami at Darul Uloom, Karachi, Pakistan. Then he specialized in Islamic Jurisprudence under the guidance of his eminent father, Mufti Muhammad Shafi, the late Grand Mufti of Pakistan. Since then, he has been teaching hadith and Fiqh at the Darul-Uloom, Karachi

Sukuk and Their Contemporary Applications

By Muhammad Taqi Usmani

In the name of Allah, the Merciful and Mercy-Giving

Introduction

Praise to Allah and only to Him!

And blessings on those of His Servants He has chosen!

As to what follows:

Among the duties of the Shariah Council, as stated in the statutes of the Accounting and Auditing Organization for Islamic Financial Institutions is the following:

> To bring about mutual conformity or approximation between the conceptualizations and the practical applications of Shariah supervisory boards of Islamic financial institutions so as to avoid inconsistencies and contradictions between the *fatawa* and the implementations of these institutions in ways that lead to the effectiveness of the role of Shariah supervisory boards in Islamic financial institutions and central banks.

Investment Sukuk worth enormous amounts have appeared in our times, and have been widely subscribed to by many Islamic banks. At the same time, many scholars have expressed their opinions in relation to the compliance of Sukuk with the precepts of the Shariah. Therefore, the Shariah Council in its prior meeting at al-Madina al-Munawwarah decided to study the subject at its next annual meeting in Makkah al-Mukarramah. As the responsibility to prepare a concise report of the issues requiring further study and debate was given to me, I have therefore prepared this modest brief as a working paper for discussion of the subject at the coming meeting, Allah willing.

All praise to Allah, Lord of All the Worlds!

Peace and Blessings upon our Leader and our Prophet, Muhammad, the Finest of the Prophets, and upon his family and Companions, and upon everyone who follows them in righteousness until the Day of Judgment!

As to what follows: The issuance of Sukuk on the basis of the rules of the Shining Shariah of Islam is among the objectives of Islamic banking, and is also one of the greatest means of establishing Islamic economies in society. This, however, is on condition that the tools used to develop and structure Sukuk are in consonance with the fundamental principles which distinguish Islamic economic systems from others. The interest-based system prevalent in the world today regularly issues

bonds that yield interest from capital-intensive enterprises that bring great profits and regular revenues. Yet, the holders of such certificates are no more than lenders to the sponsors of such enterprises; and their earnings come from the interest on their loans in a percentage that accords with the price of interest in the marketplace. The profits of these enterprises after costs, including interest payments, return exclusively to the sponsors. The basic concept behind issuing Islamic Sukuk, however, is for the holders of the Sukuk to share in the profits of large enterprises or in their revenues. If Sukuk are issued on this basis they will play a major role in the development of the Islamic banking business and thereby contribute significantly to the achievement of the noble objectives sought by the Shariah. Among the benefits of Sukuk are the following:

1. Sukuk are among the best ways of financing large enterprises that are beyond the ability of a single party to finance.
2. Sukuk provide an ideal means for investors seeking to deploy streams of capital and who require, at the same time, the ability to liquidate their positions with ease whenever the need should arise. This is because it is envisioned that a secondary market for the trading of Sukuk will develop. Thus, whenever investors require cash from their investments, or from a part of the same, it will be possible for them to sell their Sukuk holdings, or a part thereof, and receive their value from their original investment plus earnings, if the enterprise is profitable, in cash.
3. Sukuk represent an excellent way of managing liquidity for banks and Islamic financial institutions. When these are in need of disposing of excess liquidity they may purchase Sukuk; and when they are in need of liquidity, they may sell their Sukuk into the secondary market.
4. Sukuk are a means for the equitable distribution of wealth as they allow all investors to benefit from the true profits resulting from the enterprise in equal shares. In this way, wealth may circulate on a broad scale without remaining the exclusive domain of a handful of wealthy persons. This is clearly among the most important of all the higher purposes sought by an Islamic economic system.

Today, there are many Sukuk in the market, all claiming to be Islamic Sukuk. In this brief study, I mean to shed light on the mechanisms they use and on the extent to which these comply with the precepts of Islamic jurisprudence, and its principles, and its higher purposes. The issuers of these Sukuk have expended a great deal of effort to make them competitive with the conventional bonds prevalent in today's capital markets. By endowing these Sukuk with the same characteristics of bonds, they have attempted to facilitate their acceptance in both Islamic and conventional markets.

The most prominent characteristics of conventional bonds may be summarized as follows:

1. Bonds do not represent ownership on the part of the bond holders in the commercial or industrial enterprises for which the bonds were issued. Rather, they document the interest-bearing debt owed to the holders of the bonds by the issuer, the owner of the enterprise.
2. Regular interest payments are made to the bond holders. The amount of interest is determined as a percentage of the capital and not as a percentage of actual profits. Sometimes the interest is fixed, while oftentimes in bonds with longer tenors the rate of interest is allowed to float.
3. Bonds guarantee the return of principal when redeemed at maturity, regardless of whether the enterprise was profitable or otherwise.

The issuer of such bonds is not required to return more than the principal and the agreed amount of interest. Whatever profits may have been earned by the enterprise accrue entirely and exclusively to the issuer. So the bond holders have no right to seek a share in the profits beyond the interest.

These characteristics are not to be found in Islamic Sukuk, at least not directly. Even so, the issuers of Islamic Sukuk today have attempted to distinguish their Sukuk, however indirectly, with many of these same characteristics. For this reason they have developed a variety of mechanisms. Let us now study these mechanisms in the light of the following three points.

1. **Bond Holders' Ownership of Enterprise Assets**

The first point, or the bond owners' ownership of enterprise assets, is that the majority of Sukuk are clearly different in this respect from interest-based bonds. Generally, Sukuk represent ownership shares in assets that bring profits or revenues, like leased assets, or commercial or industrial enterprises, or investment vehicles that may include a number of projects. This is the one characteristic that distinguishes Sukuk from conventional bonds. However, quite recently, the market has witnessed a number of Sukuk in which there is doubt

regarding their representation of ownership. For example, the assets in the Sukuk may be shares of companies that do not confer true ownership but which merely offer Sukuk holders a right to returns. Such Sukuk are no more than the purchase of returns from shares; and this is not lawful from a Shariah perspective. Likewise, there has been a proliferation of certain Sukuk that are based on a mix of ijarah, istisna' and murabahah contracts undertaken by Islamic banks or institutions such that these are packaged and sold to Sukuk holders who hope to obtain the returns from these operations. The inclusion of murabahah contracts into such Sukuk, however, cannot but bring into question the issue of the sale of debt,3 even if the percentage of the murabahah contracts may be considerably less than that of the ijarah, musharakah and istisna' contracts. All of this requires careful review.

2. **Regular Distributions to Sukuk Holders**

In reference to the second point, most of the Sukuk that have been issued are identical to conventional bonds with regard to the distribution of profits from their enterprises at fixed percentages based on interest rates (LIBOR). In order to justify this practice, the issuers include a paragraph in the contract which states that if the actual profits from the enterprise exceed the percentage based on interest rates, then that amount of excess shall be paid in its entirety to the enterprise manager (whether a *mudarib*, or a partner, or an investment agent) as an incentive for the manager to manage effectively. I have even seen in the structure of certain Sukuk that they do not state that such excess will become the right of the manager as an incentive but, instead, they state no more than that the holders of the Sukuk will be entitled to a fixed percentage based upon the rate of interest at the time of regular distributions (as if the excess as an incentive was established by estimation or by exigency). If the actual profits are less than the prescribed percentage based on interest rates, then the manager may take it upon himself to pay out the difference (between the actual profits and the prescribed percentage) to the Sukuk holders, as an interest free loan to the Sukuk holders. Then, that loan will be recovered by the lending manager either from the amounts in excess of the interest rate during subsequent periods, or from lowering the cost of repurchasing assets at the time the Sukuk are redeemed as will be explained in detail in the third point, below, Allah willing.

3. **Guaranteeing the Return of Principal**

As to the third point, virtually all of the Sukuk issued today guarantee the return of principal to the Sukuk holders at maturity, in exactly the same way as conventional bonds. This is accomplished by means of a binding promise from either the issuer or the manager to repurchase the assets represented by the Sukuk at the stated price at which these were originally purchased by the Sukuk holders at the beginning of the process, regardless of their true or market value at maturity.

Then, by these complex mechanisms, Sukuk are able to take on the same characteristics as conventional, interest-bearing bonds since they do not return to investors more than a fixed percentage of the principal, based on interest rates, while guaranteeing the return of investors' principal at maturity.

We will now speak about these mechanisms firstly from the perspective of Islamic jurisprudence and secondly from the perspective of the higher purposes of Islamic finance and economics.

From the Shariah perspective, there are three questions:

First: Stipulating the amount in excess of the price of interest for the manager of the enterprise under the pretense that this is an incentive for good management.

Second: The manager's commitment, if the actual profits are less than the yield from the fixed rate of interest during any of the times for distribution, to lend the amount of the shortfall to the holders of the Sukuk. Thereafter the amounts of such loans will be recovered either through the actual profits of the enterprise at the times of following distributions or through the sale of the enterprise's assets at maturity.

Third: The binding promise by the manager that he will purchase the assets represented by the Sukuk at their face value, and not at their market value on the day they are redeemed.

One: Stipulating an Incentive for the Manager

With regard to the stipulation of an incentive for the manager of the enterprise, its justification may be found in what certain jurists have mentioned in regard to the lawfulness of offering incentives in contracts of *wakalah* or in brokerage. Al-Imam al-Bukhari mentioned the same on the authority of the Companion Ibn `Abbas and Ibn Sirin:

> Said Ibn `Abbas:"There is no impediment to one's saying, 'Sell this cloth and whatever is in excess of this or that4 will be yours.'" Said Ibn

> Sirin: "When someone says, 'Sell it for this much and whatever profits are realized beyond that will be yours, or will be shared between us,' then there is no problem with that."

This opinion was adopted by the Hanbali school of jurisprudence. In *Al-Kafi* by Ibn Qudama it is written:

> If someone says, "Sell this for ten, and whatever you receive in excess will be yours," then that excess will be lawful for the seller because Ibn `Abbas did not see any impediment to doing so.

This opinion is recorded by Ibn Abi Shaybah in his *Al-Musannaf* from Ibn `Abbas, Ibn Sirin, Shurayh, `Amir al-Sha`bi, al-Zuhri, and al-Hakam. `Abd al-Razzaq added Qatada and Ayyub to those who agreed. The arrangement, however, was considered *makruh* (undesirable) by Ibrahim al-Nakha`i and Hammad, as related by `Abd al-Razzaq, and by al-Hasan al-Basri and Tawus ibn Kaysan as related by Ibn Abi Shaybah. This is the opinion of the majority, other than the Hanbali scholars. Al-Hafidh Ibn Hajr commented on the opinion of Ibn `Abbas mentioned by al-Bukhari:

> This, too, refers to the wages of a broker. But, as these are unknown, the majority of jurists have not allowed the arrangement, saying if the broker sells the item for the owner on this basis, he will be entitled to no more than the fee customarily awarded for similar sales. Some jurists have interpreted the statement by Ibn `Abbas to mean that he saw the situation as analogous to that of a partnership. The same interpretation was given by Ahmad ibn Hanbal and Ishaq. Ibn al-Tin recorded that some jurists stipulated, for its acceptance as lawful, that people at the time understand the price of the goods to equal more than what was stated; but his opinion was challenged on the grounds that ignorance of the actual amount of the fee still remains.

Badr al-Din al-`Ayni wrote:

> As to the opinion of Ibn `Abbas and Ibn Sirin, well, the majority of scholars do not allow such a sale. Among those who disliked it are Sufyan al-Thawri and the jurists from Kufa. Likewise, al-Shafi`i and Malik did not allow it. If someone sells on this basis he will be entitled to a fee equal to what is customary for such a sale. Ahmad and Ishaq, however, have allowed the sale, saying, "This is actually a partnership, for at times a partner will not profit."

Of course, all of this is said in relation to the fees of a broker if other than the excess over the stated original price of the sale is not specified. However, if the broker's fee is stated as a determined amount, and then the broker is told, 'If you sell this for more than this, the excess will be yours in addition to your predetermined fee,' then it should be clear that the majority will not oppose it. This is because the ignorance with regard to the fee is lifted when it is determined in advance. Then, if the broker sells the item for more than a certain amount, the excess will be his as an incentive for better management.

On this basis, the Standard for Mudarabah approved by the Shariah Council reads as follows:

> If one of the two parties should stipulate for itself a specific amount (of profit), the mudarabah will be void. This prohibition, however, is not inclusive of an agreement by the two parties that if the profits exceed a certain percentage then one of those two parties will receive the excess exclusively such that the distribution will be according to what the two have agreed.

The operations manager in a Sukuk will manage on the basis either of its being a wage-earning employee (*ajir*) or an investment agent (*wakil*), thus resembling a broker, or on the basis of its being an investment manager (*mudarib*), or a working partner (*sharik `amil*). All of these possibilities are covered by the Standard. However, when the jurists gave permission for this arrangement, they did not consider that it would be used to carry out operations on the basis of interest rates or to maintain the status quo of the conventional, riba-based market. The right of the manager to an amount in excess of the prescribed percentage has been called an incentive for better management of the assets. Such an incentive, however, may only be understood as an incentive if it is linked to what exceeds the minimum amount of expected profits from the commercial or industrial enterprise for which tSukuk were issued. For example: if the minimum amount of expected profits is 15%, then it may be said that the actual profits in excess of that percentage may be paid the manager as an incentive. This is because that excess amount may logically be ascribed to good management. The problem is that the prescribed percentage in these Sukuk is not linked to the expected profits from the enterprise, but to the costs of financing or to the prevalent rates of interest in the market; rates that vary every day, or every hour of the day. Obviously, there is no connection between these and the profitability of the commercial or

industrial enterprise. Oftentimes, this rate will be considerably lower than the expected rate of return from the enterprise. Thus, for example, if the expected rate of return from the enterprise is 15%, the interest rate at the same time may be no more than 5%. If, owing to poor management, the actuof return from the enterprise falls to 10%, then how may what is in excess of 5%given to the manager as a reward for "good management"? How can this be, evenwhen poor management resulted in profits dipping from [an expected] 15% to onl10%? It should therefore be clear that what is being called an "incentive" in these Sukuk is not truly an incentive but rather a method for marketing these Sukuk onbasis of interest rates. It should also be clear that this aspect is not free of legal repugnance (*karahah*), even if we do not declare it prohibited (*haram)* outright.

The foregoing is from the perspective of Islamic jurisprudence only. From the perspective of the higher purposes of Islamic economics, such "incentives" in today's Sukuk actually defeat the purpose of an Islamic economic system in which wealth is equitably distributed among investors. Sukuk that are based on such "incentives" distribute profits to investors on the basis of prevalent interest rates, and not on the basis of actual returns from an enterprise.

If Shariah supervisory boards have tolerated such irregularities (*mafasid*) when Sukuk began to be issued, and at a time when Islamic financial institutions were few in number, the time has now come to revisit the matter… and to rid Sukuk from now on from such blemishes. Either Sukuk should be free of all such "incentives" or these should be based the enterprise's expected profits. These should certainly not be based on prevalent interest rates. This will then become a truly distinguishing characteristic of Islamic financial institutions, and one that sets them apart from their conventional, interest-based counterparts.

Two: Stipulating Loans when Profits Fall Below Prescribed Percentages

There is absolutely nothing in the Shariah to justify a loan when actual profits are less than the prescribed percentages. The one undertaking the loan is the operations manager, and the manager is the one that sells the assets to the Sukuk holders at the beginning of operations. If it is then stipulated that the manager will make loans to the Sukuk holders at times (for distribution) when actual returns fall below the (promised) rate of return, the transaction will come under the heading of a sale with a credit. It is well known that the Prophet, upon him be peace, prohibited sales linked to credits. The same was related by Malik in his *al-Muwatta* on the authority of trusted narrators (*balaghan*), and by Abu Dawud and al-Tirmidhi whose version reads, "A sale and a credit are not lawful." Al-Tirmidhi added, "This is a good and a sound hadith." In his commentary on this narration, Ibn `Abd al-Barr wrote:

> This hadith is recorded on the authority of `Amr ibn Shu`ayb, from his father, from his grandfather, from the Prophet, upon him be peace. It is a sound hadith that has been related by many reliable narrators on the authority of `Amr ibn Shu`ayb; and `Amr ibn Shu`ayb is a reliable narrator (i.e., his narrations are reliable) when those who relate his narrations are themselves reliable.

The entire community of scholars is agreed on this (prohibition) and no one is known to have held a dissenting opinion. Ibn Qudamah wrote:

> If someone sells on condition that the purchaser give credit (to the seller), or advance him a loan, or if the buyer stipulates the same, that will be unlawful and the sale will be void. This is the opinion of Malik and al-Shafi`i, and I know of no dissenting opinion.

At another place, he wrote:

> If he stipulates that he lease his house to him at a rate lower than the market rate, or that he take a lease on the lender's house at a rate higher than the market rate, then this will be even more unlawful.

With regard to the mechanism used in the Sukuk, the manager is not willing to offer the loan unless he receives more than his due share of the actual profits by means of the "incentive" which is stipulated for him when the percentage of actual profits exceeds the percentage based on the prevalent interest rate of interest. Therefore, such a loan, in view of the opinion voiced by Ibn Qudamah, is emphatically all the more unlawful.

At times, the manager who undertakes the loan may be a partner in the enterprise, or a *mudarib*. Such an undertaking [on his part], too, is in opposition to the requirements of the contract and falls under the same prohibition as that against a sale linked to a credit (or a loan) in exactly the same way. Thus, it is not lawful.

Three: The Manager's Promise to Repurchase Assets at Face Value

The third issue is that in true commercial enterprises, where the Shariah is concerned, the return of investors' capital cannot be guaranteed. In Shariah compliant dealings, reward

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always follows after risk. The legal presumption with regard to Sukuk is that there can be no guarantee that capital will be returned to investors. Instead, they have a right to the true value of the [Sukuk] assets, regardless of whether their value exceeds that of their face value or not. All of today's Sukuk, however, guarantee by indirect means Sukuk holders' principal. The manager pledges to the Sukuk holders that he will purchase Sukuk assets at face value upon maturity, regardless of their true value on that day. What this means is that the principal paid originally by the Sukuk holders will be returned to them at maturity. There is no other significance to such a commitment. If the enterprise is not profitable, the losses will be borne by the manager. If it is profitable, however, the profits will accrue to the manager, regardless of how great the amount. The Sukuk holders have no right to other than the return of their principal, as is the case in conventional bonds.

In considering the lawfulness of this commitment, we note that the manager of the Sukuk may act in his capacity as an investment manager, *mudarib*, for the Sukuk holders, or as a partner, *sharik*, or as an investment agent, *wakil*, for them.

A Commitment by a *Mudarib*

That such a commitment to investors on the part of a *mudarib* is void should be obvious because it is a capital guarantee by the *mudarib* to the investors, and no jurist has ever averred that such an arrangement is lawful. The Standard on Mudarabah approved by the Shariah Council states:

> If the loss at the time of closing operations is greater than the earnings, the losses will be deducted from the capital and the manager, in his capacity as a trust holder, *amin*, will not bear any of the loss as long as there is no negligence or mala fides on his part. If the costs are equal to the earnings, the investors will receive their capital back, and the *mudarib* will earn nothing. When profits are earned, these will be distributed among the two parties (investor and manager) in accordance with what the two have decided.

Thus, I can see no possible justification for such a commitment by a *mudarib*. It is, however, mentioned in some Sukuk that the manager does not make this commitment in his capacity as a *mudarib*, but in another capacity. This is clearly illogical because the *mudarib* has no other capacity in this deal.

A Commitment by a *Sharik*

The manager may also act as the partner of the Sukuk holders. Then, in the same way that it is unlawful for a *mudarib* to guarantee the return of capital to investors, it is also unlawful for one partner to guarantee the return of capital to the other partner or partners. This is because to do so would effectively interrupt the partnership in the event of losses; and that is something that no jurist has ever allowed. The Standard on Musharakah approved by the Shariah Council states:

> It is unlawful for the conditions of partnership or for the basis of profit distribution to include any text or condition that leads to the possibility that the sharing of profits will be interrupted. If this happens, the partnership will be void.

The Standard specifically mentions the unlawfulness of such a commitment in one of the following paragraphs, where it states:

> It is lawful for one of the parties to the partnership to issue a binding promise to purchase the assets of the partnership during the period of partnership or at the time of dissolution at market value or at an agreed price at the time of purchase. A promise to purchase the assets at face value, however, is unlawful.

In the Basis for Conclusions for the Standard it is stated:

> The justification for the ruling of "unlawful" with regard to the binding promise by one of the partners to purchase the assets of the partnership at face value is that this is the same as a capital guarantee, which is unlawful. The justification for a ruling of "lawful" for repurchase at market value comes from the fact that there is nothing in this arrangement that guarantees anything to the partners.

Certain contemporary scholars have attempted to justify a commitment that implies a capital guarantee by saying that while it may be prohibited in a partnership of contract, *shirkah `aqd*, it is not prohibited in a partnership of property, *shirkah milk*. They then claim that the sort of partnership that occurs in Sukuk (especially Sukuk with leased assets) is a partnership of property and not a partnership of contract. However, when we consider the reality of these two types of partnership, it is clear that the type of partnership that occurs in Sukuk is a partnership of contract and not a partnership of property. This is because the purpose of the partnership [in these Sukuk] is not merely to own physical assets for the purpose of consumption or personal benefit but for the purpose of joint investment. This is the fundamental difference between a partnership of property

and a partnership of contract.

To be more specific, when we consider what the classical jurists have mentioned regarding the reality of a partnership of contract, it should be clear to us that a partnership of contract may be distinguished from a partnership of property in three ways:

1. The purpose of the partnership of contract is to jointly seek profits; whereas the purpose of the partnership of property is no more than to have possession of something and make use of it.
2. A partnership of contract makes each partner the agent of the other in investment enterprises, whereas partners in a partnership of property are entitled to dispose of their own share [of the jointly owned property] as they wish; while they are absolute strangers with regard to the shares of the other partner or partners.
3. The partners in a partnership of contract are free to distribute profits among themselves in whatever proportion they agree among themselves. A partnership of property is different. In it, each partner is entitled only to the profits earned by his own share. So, when each partner puts his share to work separately, each partner will profit solely from the returns earned by his own share.

Each of the characteristics [of a partnership of contract] described above is to be found in Sukuk.

Shaykh Mustafa al-Zarqa', may Allah bless him, wrote clearly and concisely of the difference between the two types of partnership in what follows:

> Joint ownership always occurs in things that are shared. Such a partnership, if it occurs in physical wealth only, with no agreement as to its investment by means of a collective effort, will be called a partnership of property. This is countered by the partnership of contract in which two or more persons contract among themselves to invest wealth or labor and then to share the profits, as occurs in commercial and industrial partnerships.

At another place, the Shaykh spoke of the difference between the two types:

> The partnership of contract: This is a contract between two parties or more to cooperate on a profitable activity and to share in its profits. Partnership, in its essence, can be either a partnership of property shared between a number of persons as a result of some natural reason, such as inheritance, or it can be a partnership of contract in which a group agrees to undertake an investment activity in which they assist one another with capital or labor and then share in the results of the same. Thus, a partnership of property is a sort of joint ownership rather than anything contractual, even if the reason for the partnership may be traced back to a contract; as in the case of two people who purchase something together, so that they share its ownership. This is a partnership of property (joint ownership). There is no contract between the owners, however, to put the property to use, or to invest it through commerce or leasing or by any other means of earning profits. A partnership of contract, on the other hand, has investment and the earning of profits as its objective. This is the partnership that it intended here, and this is the partnership that is numbered among the nominate contracts, *al-`uqud al-musammah*.

Thus, the Shaykh explained that whenever the purpose of a partnership is investment or earning, regardless of whether that is to take place by means of commerce, or by means of leasing, the partnership will be a partnership of contract. Since it is obvious that the purpose of Sukuk is investment or earning by means of leasing assets, it is impossible to call Sukuk a partnership of property. Therefore, it is not lawful for one partner to guarantee the capital of another partner either directly or indirectly.

In fact, that it is unlawful for a partner or a *mudarib* to make such a commitment is a matter that requires very little in the way of justification because it is an established fact of Islamic jurisprudence that has been emphasized by fiqh academies, and at specialized seminars, and by the Shariah Council itself. If we were to open this door, the managers of Islamic banks would then be able to guarantee the capital of depositors by committing to purchase shares in investment accounts at their face value; thus negating the single difference between conventional deposits and deposits in Islamic banks.

A Commitment by an Investment Agent

In some Sukuk, the manager is neither a *mudarib* nor a partner but an agent for the Sukuk holders whose function is to invest the assets represented by the Sukuk. Then, is it lawful [for the agent/manager] to promise the Sukuk holders that he will purchase the assets at maturity for their face value? The answer is that such a commitment by an

investment agent, even if it is less egregious than a commitment by a partner or a *mudarib*, it too is unlawful. This is because agency, *wakalah*, is a contract of trust, *amanah*; and there can be no guarantees except as regards negligence or mala fides. The aforementioned commitment is tantamount to a guarantee and is therefore unlawful. This point is mentioned in para 1/2/2 of the Standard for Guarantees, issued by the Shariah Council, as follows:

> It is not lawful to stipulate a guarantee from a *mudarib*, or an investment agent, or a partner among partners, regardless of whether the guarantee is for the principal or for the profits. Likewise, an operation may not be marketed on the basis that investor capital is guaranteed.

In the following para it is written:

> It is unlawful to combine agency with a guarantee in a single transaction because to do so is contrary to the requirements of both. This is because to stipulate a guarantee by an investment agent transforms the operation into a loan with *ribawi* interest, guaranteeing [the return of] principal while offering returns from the investment.

It might, however, be imagined possible to justify such a commitment from an investment agent on the basis of an issue that was established by the Standard in the same para, where it is stated:

> However, if the agency is not encumbered by a stipulation of guarantee [or surety], and a guarantee for the agent was given in a separate agreement by another, the agent will be a guarantor, but not in his capacity as agent, such that if the agency were withdrawn he would remain a guarantor.

Then it might be said that the investment agent, though not originally a guarantor, became a guarantor as a result of the commitment which is conducted separate from the contract of agency.

The answer to this is that the proposed analogy contains a false comparison because the agent described in the Standard acts as a guarantor under a separate agreement for a debtor in the enterprise, such that the agent will not be responsible [as guarantor] unless the debtor fails to make a required payment. The agent therefore does not guarantee for the seller that his sale will be profitable under all circumstances. In the case of the Sukuk, the investment agent does not guarantee for a specific debtor, but rather against the failure of the enterprise, such that his guarantee remains valid even after every debtor has performed its obligations and the enterprise suffers losses as a result of falling prices in the market, or for any other reason. So, how can the first instance be compared to this?

Then, adding to the confusion in regard to this commitment is that the manager is the seller of the assets to the Sukuk holders, as is the case in most Sukuk, so that the commitment leads to a sale of *`iynah*. This is because he commits to buy what those to whom he has committed are selling; unless the *`iynah* is negated by means of the conditions which are well known in Islamic jurisprudence.

The Higher Purposes of Islamic Economics

To this point, this entire study has been conducted from the perspective of Islamic jurisprudence. However, if we consider the matter from the perspective of the higher purposes of Islamic law or the objectives of Islamic economics, then Sukuk in which are to be found nearly all of the characteristics of conventional bonds are inimical in every way to these higher purposes and objectives. The noble objective for which riba was prohibited is the equitable distribution among partners of revenues from commercial and industrial enterprises. The mechanisms used in Sukuk today, however, strike at the foundations of these objectives and render the Sukuk exactly the same as conventional bonds in terms of their economic results. Islamic banks were not established so that they could offer the same products, and engage in the same operations, as conventional banks in the prevalent interest-based banking system. Instead, the purpose was to gradually open up new horizons for business, commerce, and banking that would be guided by social justice in accordance with the principles established by the Shariah of Islam. Undoubtedly, such an ambitious undertaking requires a gradual approach; and a gradual approach may be imagined with a careful and detailed plan that outlines all of its various stages. Likewise, if the undertaking is to advance it will require continual follow up throughout each of its stages. A gradual approach does not mean that its progress will depend on a single step for an undetermined period of time.

Undoubtedly, Shariah supervisory boards, academic councils, and legal seminars have given permission to Islamic banks to carry out certain operations that more closely resemble stratagems than actual transactions. Such permission, however, was granted in order to facilitate, under difficult circumstances, the figurative turning of the wheels for those institutions when they were few in number [and short of capital and human resources]. It was expected that Islamic banks would progress in time to genuine operations based

on the objectives of an Islamic economic system and that they would distance themselves, even step by step, from what resembled interest-based enterprises. What is happening at the present time, however, is the opposite. Islamic financial institutions have now begun competing to present themselves with all of the same characteristics of the conventional, interest-based marketplace, and to offer new products that march backwards towards interest-based enterprises rather than away from these. Oftentimes these products are rushed to market using ploys that sound minds reject and bring laughter to enemies.

In order to promote Sukuk, the justification given is that international ratings agencies will not grant the desired, investor-grade ratings unless these mechanisms are used to guarantee the return of principal to investors, and to distribute profits from capital at specified rates. Without these mechanisms, so they say, it will not be possible to market Sukuk widely. The answer to this objection is that if we are to continue to run behind the international ratings agencies, agencies that do not distinguish between halal and haram, it will never be possible for us to move forward with authentic Islamic products which actually serve the purposes of Islamic economics. This is because these agencies have matured in an interest-based atmosphere that is unable to acknowledge the quality of an investment unless its capital is guaranteed and its returns are distributed on the basis of interest. At the same time, the quality of a product from a Shariah perspective depends upon the sharing of risk and the equitable distribution of profits between investors. Thus, the Islamic mentality is diametrically opposed to the mentality of those institutions.

As a result, Islamic Sukuk were introduced for Islamic banks and financial institutions which aim to move beyond riba. Therefore, Sukuk should be circulated among these banks on that basis. For the same reason, Sukuk should be acceptable between them so that they have no need of conventional ratings. Recently, an Islamic ratings agency was established. Islamic banks and financial institutions should strive to support that agency so that they no longer have a need for conventional ratings agencies.

Actually, the number of Islamic banks and financial institutions today is not to be overlooked, and thank God! The numbers increase day after day; and the growth of Islamic banks in many countries is greater than that of conventional banks. It is now incumbent upon these Islamic banks and financial institutions to cooperate among themselves for the purpose of developing authentic products that are far removed from empty stratagems, free from all association with riba, and that aim to serve the higher purposes of Islamic law in the spheres of economics, development, and social justice. None of this will come about without the guidance and encouragement of Shariah supervisory boards. If these boards continue with their present policies, however, Islamic banks will stumble on the road, and there is a danger, God forbid, that this virtuous movement will fail. It is time for Shariah supervisory boards to review their policies, and to moderate the license [they have granted] until now to benefit Islamic financial institutions. Instead, the Shariah supervisory boards need to apply themselves to upholding the Shariah Standards issued by the Shariah Council, standards which are not insensitive to the real needs of these institutions. Personally, I am certain that if Shariah supervisory boards uphold these Standards, the exceptional professional qualifications found in today's Islamic financial institutions will have no difficulty in developing viable alternatives to these dubious products… Allah willing.

Summary and Recommendations

1. Sukuk should be issued for new commercial and industrial ventures. If they are issued for established businesses, then the Sukuk must ensure that Sukuk holders have complete ownership in real assets.
2. The returns of enterprises should be returned to Sukuk holders regardless of what amounts they reach after costs, including the manager's fees, or the share of the *mudarib* in profits. If there is to be an incentive for a manager, then let it be based on the profits expected from the enterprise and not on the basis of an interest rate.
3. It is unlawful for a manager to lend money when actual profits are less than expected.
4. It is unlawful for a manager, whether a *mudarib* or a partner or an agent, to commit to repurchase of assets at face value. Instead, their resale must be undertaken on the basis of the net value of the assets, or at a price that is agreed upon at the time of purchase.
5. Shariah supervisory boards must abide by the Shariah Standards issued by the Shariah Council.

The New Waqf Law: A Critical Assessment

By Professor Murat Çizakça

INTRODUCTION

There is a huge need in the Islamic world to revitalize the waqf system. The currently dilapidated state of waqfs in most countries should actually be considered as an opportunity to design a thorough reform taking into consideration not only the classical Islamic waqf law but also the latest practices and norms in the west. It is to be hoped that such a synthesis of the classical Islamic and modern western practices and norms in conformity with the *Shari`ah* will lead to an ideal waqf law that can be of vital importance for the restoration of this institution.

Looked from this perspective, the IDB/IRTI and the Kuwait Public Foundation should be congratulated for preparing a waqf law to be proposed to the entire Islamic world. In what follows, I will try to assess this law from the above perspective .

The law starts with an ambitious tone and states that it will be a superior law of waqfs and any existing law in contradiction to it will be abolished. This tone is then somewhat scaled down with the statement that the preface will be written subject to the constitution of each country. If an ideal law was prepared (and I am in agreement with most of the principles of this draft law) and the whole Islamic world embraced it, this would have obviously a very positive impact. But Islamic world is a huge place and there are myriad of vested interests. Consequently, while many items of the law might be embraced, I doubt if it would be applied *in toto.* With this *caveat,* let us now look at the details.

ESTABLISHMENT

According to the classical Islamic law, a waqf is born when a wealthy person goes to the local judge, *kadi,* and declares his intention to establish a waqf. The *kadi* then records the amount of the *corpus* being donated for the purpose, subject to the condition that the capital is the private property of the founder. Thus, according to the classical tradition, there are two conditions at this initial stage; that the capital must be privately owned and that it must be registered with a local court.

Concerning registration, the IRTI-KPF draft law demands that when a person wishes to establish a new waqf, the founder must inform the local court, which will register it. The founder is also obliged to report his decision to the Association of Awqaf (The decree, item 72).

This is the traditional and, in my opinion, the correct way to establish a waqf. While I am in favour of informing the local court, the traditional method, and the Awqaf Association, I must warn against informing a state agency. History informs us that informing the state of its establishment can be detrimental for a waqf. Waqfs

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should operate as decentralized autonomous institutions without state interference.

In the United States unincorporated associations and trusts do not have to register with any state authority at all. Only incorporated associations requesting tax exempt status, need to register. The huge advantage of the American system is that it allows groups of people to meet together to pursue common purposes without having to obtain official approval or even acknowledgement. The disadvantage is that it makes it difficult to gauge the size of this sector.

The American approach is very similar to the original Islamic norm, that is the establishment with kadi`s approval alone. The New IRTI/KPF draft waqf law, correctly, provides for this. But it is important that the information given to the courts and the Awqaf Association stay with these institutions and are not conveyed to a state agency. Historical experience informs us that registration is the first step for state interference in waqf affairs.

OWNERSHIP OF THE CORPUS

Concerning the condition of private ownership of the waqf`s corpus, the IRTI/KPF draft makes clear that the endowed property must be the private property, *mulk,* of the founder (Item 6). 4

During the last century this condition has been relaxed when Iran confiscated the late Shah's property and established new waqfs with it. In Turkey and Malaysia also the state became an active waqf founder. There is nothing wrong with this, providing the state established waqf has complete independence from the very state that has established it. On this issue, I would like to point out to the establishment of the Stiftung Volkswagenwerke in Germany. After the Second World War, two states, the state of Niedersachsen and the federal one, agreed to establish with the capital of the Volkswagenwerke, which they owned, a Stiftung, foundation, for promoting scientific research. Although established with state money, the complete independence of the foundation from state interference was planned with great care. In short, establishment of a foundation with state money might be acceptable providing the foundation is granted complete independence from the very state that establishes it. If this is not provided, the foundation can be impeded by bureaucratic inertia, even, corruption. The draft, correctly, allowed the endowment of only privately owned property. But this may create problems with the waqfs whose capital are state owned. While the law makers might allow for such waqfs, it is imperative that the law also insists on their independent and autonomous management.

TYPES OF WAQFS

The IRTI/KPF draft law recognizes primarily the following three waqf types (Item 2):

a) waqf khayri, charitable waqfs
b) waqf ahli, family waqfs and
c) hybrid waqfs.

Thus, family waqfs abolished in much of the Islamic world under the pressure of the colonial powers during the 19th and 20th centuries are now being re-established. This is clearly an important development. While this is so, the draft needs to take into consideration the following types as well.

d) Incorporated waqfs: These are waqfs that enjoy full incorporate status. Thus they can sue and be sued. They also provide full owner and entity shielding to their trustees. In the United States, such foundations enjoy full tax-exemption.
e) There are six types of waqfs that are officially recognized by the latest waqf regulation of 2008 in Turkey. Referring only to the most important ones;

1) *Mazbut vakıflar* are those that survived from Ottoman era. Not having their original founders or their descendants as their trustees, they are managed by the General Directorate of Waqfs. The IRTI/KPF draft should recognize such waqfs. Indeed, what happens when the founders and their descendants disappear? Since waqfs are essentially perpetual institutions, such a possibility must be seriously considered. Such waqfs need a central authority to manage them. Within the framework of the IRTI/KPF draft, it is the Association of Awqaf which should provide this.
2) *Mülhak Vakıflar* are those that are still managed by their original founders or their descendants. As mentioned above, such waqfs should enjoy full incorporation with owner/entity shielding as well as full tax-exemption. The third and fourth categories represent Ottoman practice being reflected in modern republican norms.
3) *Mukataali Vakıflar* pertain to properties built upon waqf lands. Originally accepted by the Hanbelis, this waqf type also known as *Hukr,* has been eventually accepted by all schools. The Lebanese law of Real Estate Ownership refers to this as *muqata`a ijarah tavilah.* The *modus operandi* of these waqfs is as follows: the land is the property of the waqf and a developer rents this waqf land on the basis of *ijarah tavilah,* long term rent. Leasing waqf property for the long term is usually not permitted, but *Hukr* constitutes an exception. The developer rents the land on long

term basis and builds upon it. The building belongs to the developer and as long as he pays his rent for the land regularly, he enjoys full ownership rights over the building he has built. The developer enjoys this right for as long as he lives and he can even transfer it to his descendants.

Concerning the level of rent, two factors are important. First, the rent paid by the developer should not be lower than the prevailing rent, *ajr misl,* paid by other tenants in the neighbourhood. Second, if the neighbourhood of the leased property develops, the original rent agreed upon can be increased.

This classical arrangement has recently been somewhat changed in Turkey so as to enable the land owner (waqf) to enjoy greater income. When a developer wishes to build upon waqf land, the ownership of these properties are split between the waqf, owner of the land, and the developer who built and developed this land usually into residences or shopping centers or a combination of both. The exact ratio of ownership of the developed property, i.e., number of flats, is determined as a result of bargaining and the waqf receives annual rent from the units it owns.

The new draft law should take into consideration both the classical *Hukr* and its modern version, flat sharing, described above. This is because, the latter provides higher revenue for the waqf than the former, whereby the waqf receives rent from the developed property instead of the undeveloped land.

Mukataalı Vakıflar may well be highly relevant for contemporary Malaysia, where waqf assets with development potential are estimated to be about 40 billion RMs (12.5 billion USD), which may well dwarf most other asset forms managed by the Islamic finance industry.

4) *Icareteynli Vakıflar* are defined by the Turkish Waqf Law of 2008 as those waqf properties rented out on long term basis, without any fixed term. This category was invented by Ottomans when waqf properties were destroyed by earthquakes or fires. Faced with such disasters, tenants were asked to make a large lump sum payment, which the waqf used for rebuilding the premises. The tenants were then given long term rent contracts and continued paying their usual rents. What the tenants gained in this process was a status of quasi ownership, which allowed them to continue using the premises for the long term subject to the payment of annual rents, while the waqf was enabled to rebuild its premises.

There are number of serious objections to the *ijaratayn* arrangement. First, the exact period of the long term rent is unclear. Second, the annual rent tenants continued paying often tended to become less than the prevailing rent in the neighbourhood, *ajr misl.* Third, the fact that the descendants of the tenant can take over the property, thus diluting the property right of the waqf even further. In view of these serious objections, it is difficult to recommend that this lease form be included in the new draft law. But on the other hand, the problem of what happens to the waqf property in case of a natural disaster needs to be taken into consideration. One possible way out of this problem can be the modern *takaful*, or Islamic insurance.

THE NATURE OF THE *CORPUS*

The next question concerns the nature of the capital, *corpus,* with which the waqf is established. Classical Islamic law recognizes primarily real estate waqfs. Waqfs established with cash were discussed and permitted by Imam Zufar back in the eighth century, subject to the condition that the cash capital of the waqf should be invested in *mudaraba* partnerships and the returns spent for the purpose of the waqf. Wide spread application, however, and then not exactly remaining true to Imam Zufar`s *mudaraba* formula, was observed first in the Ottoman empire during the fifteenth century as an informal practice. These waqfs then became very popular, which triggered a long lasting debate. Finally, they were formally permitted during the late sixteenth century by a sultanic decree, thus becoming a norm. Initially limited to the Ottoman Empire, they were eventually approved in Egypt, Iran as well as in the Indian sub -continent with a long delay at the beginning of the 20th century. Moreover, this approval covered not only cash, pure and simple, but also shares of joint stock companies. Such waqfs are now known as waqf of stocks.

The importance of the waqf of stocks should not be underestimated. The Ottoman cash waqfs invested their *corpus* with a financial method known as *istiglal.* This was a legal trick designed to disguise the rate of interest embodied. Modern waqfs of stocks, however, operate with shares of various companies, a method very similar to the *mudaraba* partnership practiced by the Prophet and demanded by Imam Zufar. Put differently, waqfs of stocks are truly profit

and loss sharing partnerships, practiced and recommended by the Prophet himself.

Items 20, 21 and 22 of the procedural appendix, correctly, permit the establishment of a waqf with cash or company shares. Company shares can be endowed as the corpus of a waqf. The procedural appendix makes it clear that stocks are not for speculation but for the keeping. The trustee is not permitted to sell the stocks unless he is authorized to perform *istibdal.* Waqf of stocks is now granted definitive legitimacy. Thus the centuries old debate on the legitimacy of cash waqfs is now brought to an end thanks to the waqf of stocks. To my knowledge, the earliest approval of establishing a waqf with company shares as well as European perpetual bonds (*rente*) had been granted back in 1907 when the "Mujtahid of Karbala" granted his approval for the waqf of stocks established with such instruments. This was followed in 1908 by the fatwa of the Mufti of Egypt based on the condition that such waqfs should be divided into shares which should be handed over to the trustee. Thus, following the footsteps of these early 20th century fetvas, with the new draft law we have the definitive approval of waqf of stocks for the entire Islamic world.

In Turkey, in an effort to curb waqf founding, a paid in capital condition of at least 500,000 USD was imposed by a hostile government to anyone desiring to establish a waqf. Founders reacted to this by capital pooling. Recent research has shown that on average 35 persons founded a waqf, pooling among themselves the necessary capital. Most recently, in 2009, this requirement has been reduced to 50,000TLs by the newly established Board of Waqfs. Remarkably, after this ruling an improvement in the number of waqfs established has not been observed in Turkey, indicating that other more important factors, such as inadequate tax exemption, continue to play a negative role in this process.

Item 71 of the IDB/IRTI and the KPF Draft Law permits the establishment of a waqf by a group of founders. In view of above, I am in complete agreement with this. At this point the question comes to mind whether the law should impose any minimum capital condition to avoid the emergence of too small waqfs and to encourage capital pooling among the founders.

Currently, in Europe, there is a bewildering variety of rules regarding minimum capital needed to establish a foundation. European Union member countries demand from € 240 Euros (in Malta) to € 70,000 in Austria. In France, though there is no legal obligation, in reality, authorities insist on the ridiculously high amount of € 1,000,000. In the forthcoming *European Law of Foundations*, the founding assets must be equivalent to at least 25,000 euros, allowing the *corpus* in the form of real estate, cash, shares or a combination of all.

As the French example given above should demonstrate, imposition of any minimum capital condition can be exploited by a hostile state by pulling the amount to ridiculous heights. Moreover, the exact amount should depend on the general conditions and GNP/capita of the country in question! The authors of the law have therefore wisely refrained from imposing any such condition.

LEGAL PERSONALITY

Although the classical Islamic law does not clearly define this concept, jurists have long considered waqfs as entities with legal personality. Modern Muslim jurists like Zahraa, Zarqa and Sanusi are unanimous that the classical Islamic law, in fact, recognizes the concept. While this may well be so, it is not clear to what extent the classical Islamic law provides owner/entity shielding, both very important characteristics of the modern corporation. The most recent Turkish law of waqfs clearly grant legal personality to waqfs.

All western laws also grant this status to foundations.

With the new IDB/IRTI-KPF draft law, waqfs are now granted legal personality. The new law, however, does not make it clear whether "owner and entity shielding" are provided. More work on this is needed.

TAX EXEMPTION

In modern times, all American public serving foundations are tax exempt, while member serving ones are not. The former also receive tax deductible gifts from individuals and corporations. To be eligible for this privilege, they have to serve recognized public purposes. In 1996, Americans contributed 139 billion USDs and 85 percent of these donations and gifts came from individuals, while only six percent came from corporations. The remaining nine percent came from other foundations. About half of these donations and gifts went to religious organizations while about 12.7 billions went to education.

In the Islamic world, waqfs are, by definition, public serving. Even family waqfs become public serving entities when the family becomes extinct. Therefore, all waqfs, including the family waqfs, must be tax exempt. Because, thanks to their perpetuity, they represent sustained capital accumulation for serving the public.

In Turkey, however, tax exemption is only rarely granted. Only 2.7 to 4.5 percent of the waqfs established during the republican era have been granted tax exempt status and 24 percent of the such privileged ones are public waqfs. Recent research has revealed the very negative role of this situation

on waqf founding. Asked whether the current state imposed rules and regulations impede waqf activities, 65 per cent of the trustees said, "yes". Difficulties encountered in obtaining tax exempt status were the most cited impediment.

In the European Union, each country has its own practices and norms regarding tax exemption leading to a bewildering variety. Even the most recent, forthcoming, *European Foundation Proposal* has not remedied this situation as it has allowed each country to apply its own norms. About half of the European countries tax their foundations.

Donations constitute another important source of income for waqfs in Turkey. Of the 237 waqfs questioned in 2002, while 45 per cent received less than USD 12,000, some 33 per cent received between 12,000 and 48,000. Waqfs receiving these donations do not pay income as well as inheritance taxes in Turkey. This is the same in all European countries with the exception of Denmark, where only some reductions are allowed. For donors, however, a different situation prevails. In Turkey, a donor can deduct his donation, merely upto 5 per cent, off his taxable income.

When receiving donations, waqfs should not pay any taxes. This is the European norm. Equally important, donors should be permitted to deduct the whole of their donation from their taxable income.

Since the overall purpose of the IDB/IRTI and KPF draft law is to encourage waqfs in the Islamic world, tax exemption appears to be a very important concern. This is confirmed by the Turkish situation explained above.

Item 62 of the draft law exempts all charitable waqfs (khayri) from all taxation. This is a necessary but insufficient condition. Since waqfs are nonprofit organizations channelling all of their earnings, minus expenses, to charitable purposes, any tax imposed on them simply reduces the funds that could have been spent for these purposes. Tax exemption needs to be considered at three different levels: taxes imposed directly on the revenues generated by waqfs, taxes imposed on donors and finally, those imposed upon the profits generated by companies associated with waqfs. The draft law should recognize the need for all of these and provide tax exemption at all three levels.

Moreover, while the draft law exempts charitable waqfs from taxation, it is silent about family waqfs. Since family waqfs are potential charitable waqfs in that they will convert into charitable waqfs when the family they are designed to support becomes extinct, they should be granted the same tax status as charitable waqfs.

SOURCES OF INCOME

As mentioned above, while Ottoman cash waqfs earned their income by lending their original capital with *istiglal,* quasi interest, modern waqfs of stocks obtain shares of joint-stock companies and thus become true partners of professionally managed firms ultimately sharing risks, profits and losses.

With the exception of the Czech Republic, all the members of the European Union allow their foundations to establish associated companies. So, this is the European norm.

Modern waqfs of stocks can also establish their own firms. Indeed, Turkish waqfs were allowed to establish associated companies already back in 1967. Currently, 24 per cent of Turkish waqfs possess commercial firms. A small group of these waqfs earned on average exceptionally high USD 400,000 annual revenue. Most, 70 per cent, however, earned less than USD 48,000 per annum. On the whole, 81 per cent of Turkish waqfs are reported to enjoy profits, which they either distribute as charity or add to their capital. Commercial revenue constitutes 42 per cent of Turkish waqfs' annual income, and is taxed.

While the IDB/IRTI and KPF draft law allows waqfs to obtain shares of various companies (procedural appendix, item 208), the draft is silent about waqfs actually establishing their own firms. This should be permitted just as companies establishing their own waqfs should also be permitted. Such flexibility enriches the waqf sector.

WAQF DURATION AND REVOCABILITY

Waqfs are generally known as perpetual institutions. Indeed, it is possible to find waqfs that have survived for centuries all over the Islamic world. The new IDB/IRTI and KPF draft law, however, has permitted establishment of fixed duration waqfs. Family waqfs are considered to be temporary waqfs (Draft Law item: 70/3; Appendix item 64). Although, the purpose is to make waqf establishment attractive, the word of the law is ambiguous here.

In the same context, revocability is also permitted subject to certain conditions. Indeed, the founder can change his mind and revoke his waqf. This rule settles another debate in classical waqf law which had led to a cumbersome procedure for waqf establishment in Ottoman era.

TRUSTEES

The law (24/2, appendix item 111) makes it clear that the trustee(s) are to be appointed by the founder. This condition is well known and reflects the classical law as well as centuries` long tradition. Yet, it challenges the current situation in Malaysia where the state religious councils are the sole trustees of all the waqfs in a given state. If this law is

accepted in Malaysia, it can make the previous law null and void per item one above.

One of the novel items of the new draft law is that it permits the determination of the trustee's wage by the founder as a certain percentage of the waqf's profit or revenue (appendix, #137). Linking the trustee`s wage to the profitability of the waqf rather than making it a fixed monthly sum, this item makes the trustee strongly interested in the performance of the waqf. I consider this as a very important development in view of many critiques of waqfs in history, whereby this institution was labelled as the dead hand. Linking the trustees` income to the performance of the waqf should no doubt make these institutions more dynamic.

There is concrete evidence to support this view. Sadr and Souri have studied the rental income generated by waqf owned stores in the grand bazaar of Teheran. Their conclusion is startling: Of the three categories of waqfs they consider: those whose trustees are selected directly by the founder; those appointed according to the will of the founder and those directly administered by the Awqaf Organization, the average rental income of the stores in the bazaar administered by trustees appointed by the founder is 99.3, by the trustees appointed according to the founder`s will is 101.5 and administered by the Awqaf Organization is 34.7 thousand Rials respectively. The income of the first two categories, both run independently of the AO is almost three times of those run directly by the AO. This is despite the fact that the wages of the trustees of the first two categories are only indirectly linked to the performance of the waqfs they manage.

A policy suggestion can be drawn from this, centralised awqaf organizations are necessary, particularly in view of waqfs whose founders have perished. But they should not be involved in direct day to day management. Instead they should quickly hand over the waqfs under their management to selected trustees whose income are directly linked to the performance of the waqfs they manage. Looked from this perspective, appendix number 137`s importance becomes obvious.

INVESTMENT

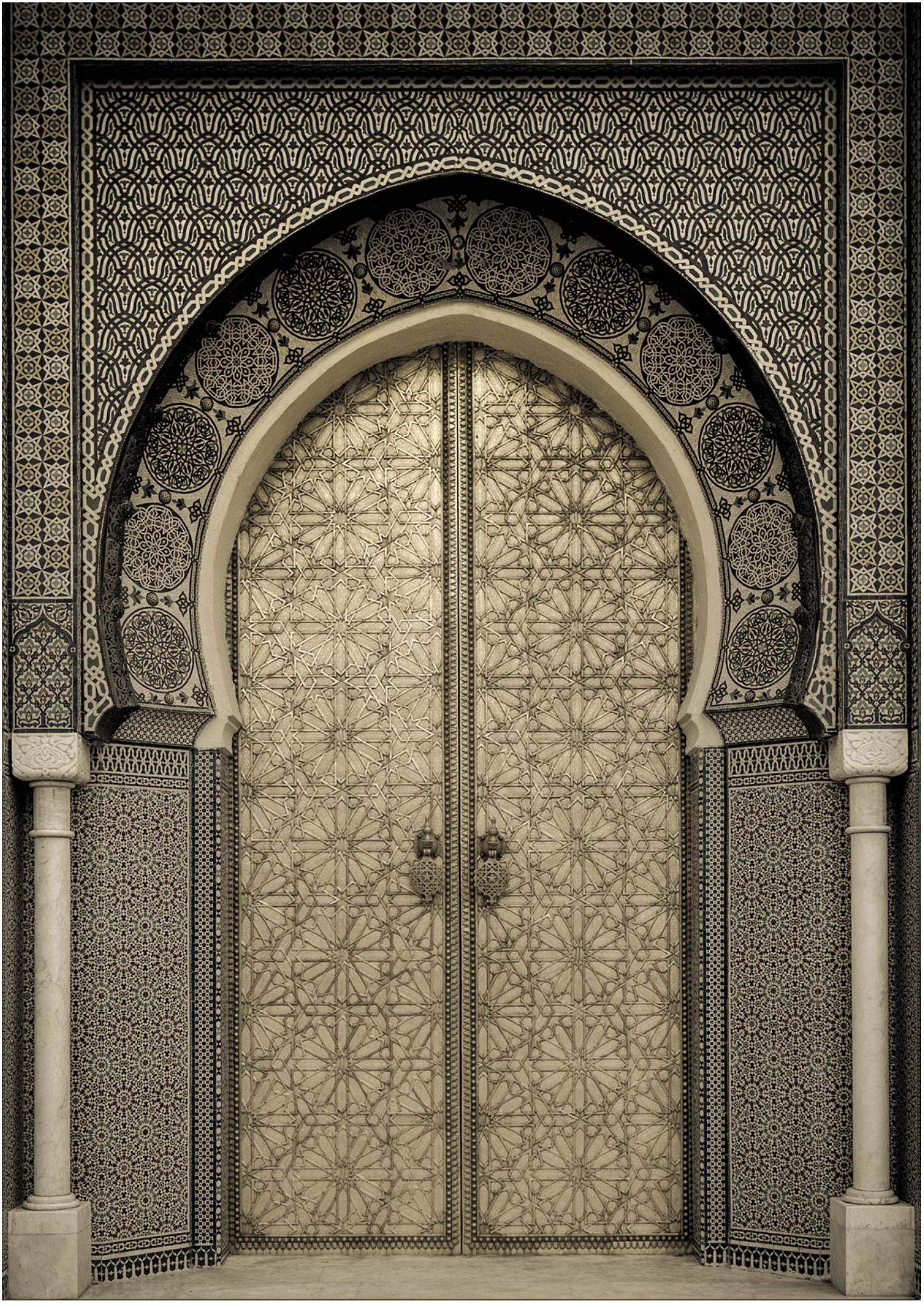
The following Islamic partnership forms are considered by the law (Appendix #208) as appropriate methods of investment of the *corpus:*

a) *Mudaraba.*
   The draft law allows even the risky *mudaraba* thus confirming Imam Zufar`s original ruling back in the eighth century that was hardly ever practiced. This is a revolutionary permission and should be applauded. It combines mudaraba with waqf – two powerful institutions. This constitutes the ultimate support given to entrepreneurship as waqf funds constitute long term funds, exactly what entrepreneurs need. This is a revolutionary step. Indeed, permitting waqf funds to be invested in *mudaraba* partnerships opens the way for venture capital type of investments thus facilitating the birth of this important sector in the Islamic world.
b) Musharakah mutanakisa
c) Leasing
d) Ijaratayn, thus confirming the centuries' long Ottoman practice
e) Joint-stock company shares, confirming the 1907 and 1908 fatwas. But these fatwas had also permitted perpetual bonds as waqf *corpus.* Islamic perpetual bonds, *esham,* should also be accepted as waqf *corpus* as they are Shari`ah based and are not involved in riba.
f) Islamic investment funds
g) Investment accounts in Islamic banks
h) *Mudaraba* accounts with Islamic banks
i) *Istisna'a*
j) *Mudaraba* within *Istisna'a*
k) *Murabaha*
l) *Muzara'a*

Finally, a suggestion: Although the classical law demands so, the amount a donor wishes to donate should not be limited to one third of his wealth. After all, Shari`ah permits *hiba* without any limit. Put differently, a person while healthy, can give his entire wealth as a gift to any person. The only condition being that the beneficiary actually receives it. Thus the one-third limit can and should be exceeded with the new law. After all, in the United States, Bill Gates and Warren Buffet donated 90 per cent of their wealth. Are Muslims less altruistic than these Americans?

CONCLUSION:

Within the time limit I was given, I have been able to pinpoint only to some of the salient points of the IDB/IRTI and KPF draft law. Subject to the caveats and suggestions I have made, my overall impression of this draft law is highly positive. If the draft, indeed, becomes a universal law of waqfs, its authors would have done a great service to the Islamic world.



Interview with Prof. Laurent Marliere

CEO of ISFIN

By Alberto Di Gennaro

Prof. Laurent Marliere Professor of Marketing - Ceo of ISFIN - Islamic Finance and Markets - Global expert in marketing for professional firms. Laurent Marliere is an acknowledged observer of the ISLAMIC Economy and HALAL industry. He frequently speaks at forums in Asia and the Middle East on how to accompany companies in developing a Halal capacity for their conventional products

Can Dubai Become the Capital of the Islamic Economy?

Q: What is the Islamic economy?

A: The term Islamic economy can be considered through various angles. Minimalists would say it refers to the economies of the 57 member states of the Organisation of Islamic Cooperation (OIC) or to products defined by Sharia compliance, such as finance and food. Maximalists believe it is one segment of the global economy, which focuses on Islamic consumers, regardless of location. I personally follow the approach focused on the consumer and demand. Islam and Muslims are a global paradigm with specific needs and requirements that need to be serviced accordingly. The fact that large forums like the World Islamic Economic Forum (WIEF) hold their annual gatherings in non-Muslim countries is evidence that the Islamic economy is a worldwide phenomenon. In Asia, people tend to refer to the "Halal industry" to describe the Islamic economy.

From a commercial perspective, the Islamic economy encompasses products and services driven by the Muslim consumer's adherence to some form of faith-based activity. The scale of value depends on the level of faith and the market sector: ranging from pure Sharia compliance to Sharia friendliness. Core sectors of the Islamic economy are, of course, the Halal food sector and Islamic finance. They are the visible part of an "Halal" iceberg that includes a wide range of sectors like personal care & cosmetics, pharmaceuticals, travel & leisure, banking, insurance, transport & logistics, fashion & lifestyle, media, professional services, consultancy, and others.

In terms of figures, one could consider the 1,65 billion Muslims who constitute the Ummah as the market of the Islamic economy. I ponder this, as Muslims across the world are heterogeneous in their consumption habits and, besides, Islamic products could also be potentially interesting to non-Muslims.

According to an insightful survey conducted by Thomson Reuters in 2013, the global expenditure of Muslim consumers on food and lifestyle sectors was $1.62 trillion in 2012 and expected to reach $2.47 trillion by 2018. Islamic financial assets in 2012 were estimated at $1.35 trillion in total disclosed assets and growing at 15-20% a year in most core markets. This report estimates the potential value of Islamic banking assets in its core markets to be $4.1 trillion.

Q: What is the main challenge of the Islamic economy?

A: The main challenge is the lack of understanding of the Muslim consumer and their needs. Economic and political actors have clearly understood the potential of the Islamic community of consumers and speak in their name but the reality on the ground is very different.

Islamic finance, which is one of the most mature sectors of the Islamic economy, is unable to make a real breakthrough because of the very fact that it is industry-driven and not market-driven. Financial institutions like *Noor Islamic* have erased the term "Islamic" from their brand, *HSBC Amanah* no longer offer Sharia-compliant products and services in the UAE and the UK and the *Islamic Bank of Britain (IBB)* encounters profitability issues.

At a recent conference held in Dubai on how to develop Islamic finance in Africa, there were no Africans in the panel or in the room…

Let us draw a historical parallel with the "conventional economy". In the 1970s, the West was producing junk items and services and using publicity to sell them to consumers who were treated like sheep. We lived then in the so-called "production economy" that eventually led to the consumerist movement. Consumers organised themselves and forced the industry to produce according to their needs and demands. We stepped in the "consumption economy". In my opinion, the young Islamic economy is in many ways still a "production economy".

Q: Why Dubai?

A: The vision of His Highness Sheikh Mohammed Bin Rashid Al Maktoum, the Vice President and Prime Minister of the United Arab Emirates and Ruler of Dubai, to transform Dubai

into the capital of the Islamic economy has given a different resonance to this fast-growing sector of global economy. Observers throughout the world know that Dubai and its authorities have the capacity to pool the means to achieve such ambitious plans.

Dubai has indeed a row of strengths to take on that status. However, several challenges and weaknesses have to be met and handled carefully.

Q: What are Dubai's strengths?

A: The vision. The Islamic economy is one of the most innovative segments of the world's economy. It still needs to be conceptualised and therefore offers tremendous opportunities for an authority with sound leadership. The fact that this initiative has been launched with enthusiasm at the highest level of the government, gives a strong and credible signal to the world.

The means and faith. Dubai has proved in recent years that it has the capacity to handle financial challenges and great infrastructure projects. If the vision is backed by the righteous means both in terms of finance and knowledge, the rise of Dubai as key player of the sector can be achieved. International macro financial institutions like the Islamic Development Bank (IDB) or the World Bank should step into the project.

The geography. The world map is no longer focused on the Atlantic or the link between the US and Europe. The new planisphere is focused on the Pacific and makes Dubai a potential regional capital, a metropolis of Asia and, perhaps even the business capital of Africa, which fails to develop a secure centre. The geo-economics of Dubai makes it more accessible than Malaysia from Europe and easily reachable to the Muslim populations of Africa, the Levant, the GCC and Asia.

The business culture. The Islamic economy does not solely belong to Muslims. It is a universal industry segment. Dubai has managed to combine an Eastern and Western cosmopolitan culture, which makes it easier to carry out business and trade than in other neighbouring countries.

The rule of law. The legal and judiciary systems in Dubai guarantee the necessary security for business and FDI.

The blank page. Starting from scratch is a strength: everything can be invented! However, it would be unwise to simply mimic what others have done. Merely copying what Malaysia has done is unrealistic because the Malaysian model, although a great lesson to the world, is not a complete success since it has not managed to conquer more than a regional space! It has failed to become global.

Tax incentives. To become a capital, Dubai is going to need to attract new companies, corporations and investors to its soil. Tax can play a decisive role. Dubai authorities may underestimate that factor, as it appears exotic to their local daily life. However, tax pressures in the West are climbing at the same time as traditional tax havens are under scrutiny and pressured by strong political and legal measures, mainly issued by the US and the UK (Fatca legislations, etc.), whose citizens are heavy users.

In most off-shore jurisdictions, one only finds a tax haven and a beach haven. In Dubai, you find a tax haven, a beach haven and a trade haven… a real added value for many Western corporations willing to relocate.

If handled properly, and kept an "on-shore" jurisdiction, Dubai and the UAE can pretty much play the role of Luxembourg in the European Union. The GCC will increase its integration in the coming years, like the EU did. Dubai can be a competitive player in this economic union.

Professional services. The development of the Islamic economy will require support services of high standards which are available in numbers in Dubai, such as law firms, audit & accounting services, banks, certificatory bodies, and brokers.

Dubai can use the professional services firms' home networks and client portfolios to facilitate the relocations of their clients to the Dubai International Financial Centre (DIFC) and elsewhere. There are 68 international law firms and 400 banks there already. There is great potential to create a spider effect boosted by tax incentives.

A fish is not necessary halal. We live in a complex and sophisticated world. What was halal yesterday might not be today. Take the example of a fish: today, it can be raised on a fishing farm and fed a cocktail containing pork meat, wrapped in a pack full of alcohol-based ingredients and transported in a container that carried haram products the day before. The process of halalization can become universal, as can the demand. It is linked to the supply chain of the products. Dubai becoming a logistical hub means it can take a share in a "supply chain model 2.0", tailored to the halal industry.

Q: What are Dubai's challenges?

Gadgetisation. A short-term or even mid-term view is problematic.

If the sole aim is to make Dubai a nice-looking fiancée to

present at the World Islamic Economic Forum (WIEF) in October then you risk building on sand instead of concrete. The project deserves, and requires, a long-term plan based on pillars that will explain what the Islamic economy will be in 10 or 20 years!

A myopic short-term plan to simply state that "we are the capital" is not enough. A careful strategic analysis on how to sustain this leadership position needs to be implemented.

In such a huge macroeconomic project, the micro management of smaller items can carry people away – that's what I call the camel view! But success requires a falcon view from the top down…

People need to be realistic on the calendar and agenda. It should take at least a year to create a solid roadmap. Before you build a Burj Khalifa, architects require time to plan the work of art. Otherwise, you create a mere gadget and risk disappointing or upsetting people. Many observers in the Muslim world are now looking at Dubai with a smile on their face. Will the promise be kept? What will be the outcome?

Duplicating the mistakes of the Islamic finance industry. Islamic finance is a mix of money and regulations. It should be a mix of money, marketing and fewer regulations. It is likely that the Islamic economy embarks on a similar journey, where simple things are made complicated by regulators, lawyers and scholars, carrying away the one who should be the real beneficiary of the Islamic economy: the consumer!

The Islamic financial industry is struggling with its products and needs some clearly-defined directions, or strong recommendations, to address major issues: its growth and profitability.

The market positioning of the majority of Islamic products is religious, not financial. Hence, IFF (Islamic Financial Institutions) are failing to penetrate into the mass segments of the Muslim consumers, let alone attracting non-Muslim customers. The religious positioning of the products helps them attract the religious segment, which is thin and shallow. Once this segment is exhausted, institutions find it very hard to penetrate the remaining segments of the market, including the most valuable segments. Religious consumers buy conventional products because they do not see the value of the Sharia-compliance of the product.

Dubai should learn from the mistakes of the Islamic finance industry and launch a smarter paradigm.

Customer is mufti! I have addressed this fundamental issue before: the Islamic economy cannot be based on what regulators see fit, but on the needs expressed by consumers. We will see the rise of Islamic consumerism, which will shape the halal industry and the Islamic economy.

Global scale. The Islamic economy goes beyond Islamic countries. It is a *de facto* global endeavour, as most suppliers to the Islamic markets are based in the West! Besides (although it should not be overestimated) the relevance of halal products can be attractive to non-Muslim consumers.

There are four market "circles" to consider:

Circle 1 is the worldwide market of suppliers and buyers.

Circle 2 is the Islamic markets of suppliers and buyers.

Circle 3 is the GCC.

Circle 4 is the UAE.

Looking only at circles 3 and 4 would be shortsighted.

Cultural heterogeneity. Becoming a global economic capital implies that you have a hinterland. 65% of Muslims are Asians. Dubai is an Arabic market. Islam unites them, but Muslims differ in their economic behaviour according to their cultural origin. In order to tap into the substantial Asian markets, Dubai will need to submit a tailor-made offer to that market or play the card of universality.

Missing out on useful sectors. Based on the report provided by Thomson Reuters, which strongly influences the Dubai authorities, seven strategic sectors have been chosen. I personally think that the Islamic economy is much broader than these sectors and that it is too limiting to restrict it to those chapters. Although relevant, these seven sectors exclude other key areas, which make up the Islamic industry.

If it is an economic choice to limit Dubai's area of influence to these sectors, then it is a strategic choice and, although questionable, it is conceivable. But from a scientific point of view, what I call the "halalization" of the industry will imply far more dimensions which should not be ignored.

Fragmentation. The sectors of the Islamic economy belong to a unit, which is the set of values behind it and the market it addresses. Separating them and running them independently of each other is unwise.

Education. Succeeding in the Islamic economy implies success in the academic sector. One should not confuse information and education. Dubai can buy or attract all necessary information and data suppliers to its soil, but building a first-class academic system is a very different story. The fact is that other "Islamic hubs" have much stronger academic records and highly ranked institutions. These universities or business schools provide an elite who can manage the different chapters of the industry. They

provide in-depth and long-term strategic thinking and development of products that cannot necessarily be provided by commercially-minded information suppliers.

There are three levels of education Dubai needs to develop:

Level 1 is vocational and professional training. The purpose is a short-term upgrade of industry executives to lead their business into the Islamic economy. These entrepreneurs have their own business plan but don't understand what the Islamic economy is about. Everybody wants a share of the industry but nobody knows how to do it.

Level 2 is higher education. Train skilled graduates to take on active roles in the new industry and generate PhD students who will form an academic intelligentsia for Dubai.

LEVEL 3 is basic education (A level & O level). The purpose is to make high school children learn the basics of the industry so they may later consider it as career option.

The Islamic economy needs to be built. This requires content, which in turn requires strong academic relays. Building such an education system will not happen in 3 years… So you have to look at the matter from a long-term perspective.

Sheikh-size bed. Dubai has proved that it can see BIG! It has to create the standard in the Islamic economy and invent a new paradigm in the halal industry. A "Sheikh-size bed" must be bigger than a "King-size bed"!

Unlike many local observers, I do not believe that Dubai will beat London in the near future as the capital of Islamic finance. The City of London still has some assets and the historical status of world capital that Dubai has not yet achieved. But in the segment of the Islamic economy, Dubai can definitely become the leader provided that its authorities fuel the proper resources and intelligence into the project. If Dubai becomes the world capital of the Islamic economy than it can become the world capital of Islamic finance… not the other way around.

Execution. Clearly, Dubai has set an exciting and challenging mandate for itself. Success for Dubai will raise the performance bar across the Islamic markets internationally. The primary risk however will remain the execution and implementation of a great theoretical challenge.

Q: Where does your interest for the Islamic markets come from?

My DNA is strategic marketing. While analysing global market trends in 2010, I realised that one consumer out of four in the world is not served according to their needs. That consumer is the Muslim consumer. Marketing, when conducted ethically, is a remarkable tool to improve people's life. My humble job is to seek pragmatic ways to formalise the Islamic industry for the benefit of the consumer... and the supplier. This creates a better marketplace.

What future for Italy and Islamic finance?

By Stefano Padovani

If the theme of the relation between economy and ethics cuts across all the great religions, in the Muslim religion all the economy is permeated by moral principles. In particular, the Koranic prohibitions of usury and transaction risks are applied in all countries, in that valid for each believer, wherever he/she is. We can say that this is an "*ante-litteram*" ethical finance that must be faced today if we consider a few macroeconomic and demographic figures: according to current projections, in 2025 about one third of the world's population will be of Muslim faith (2.5 billion), 65% of Muslims live in Asia (with a strong presence in India and China) and 40 million Muslims live in the EU. At a time when economic growth tends more and more to move from West to East, not to deal with this phenomenon - especially for a country in deep recession for several years and with a significant need to attract foreign investors such as Italy - would mean losing a great opportunity. Finance is just one aspect of the Muslim economy (the so-called "*halal industry*", from "*halal*", the opposite of "*harar*", which means the prohibition of unethical behaviours including gambling, the production and consumption of alcoholic beverages, pork products, pornography, etc...) that extends to sectors such as food, cosmetics, bio-pharma, transport, education, lifestyle and many more, with a value of about 2300 billion dollars per year and a 10% growth rate. Among the European countries in the forefront of the issue on Islamic finance, there are the United Kingdom, which will be the first country outside of the Muslim world to finance itself through the *sukuk*, the so-called Islamic bonds (asset or cash flow-based securities that give the investor a share in the underlying investment with a preset yield or a sharing in profits and losses) and Luxembourg, at whose stock exchange approximately 16 issues of *sukuk* are already listed. And Italy? Even with the presence of about 1.3 million Muslim residents and its geographical position that makes it a natural bridge between Europe and the Arab world, and albeit the phenomenon of Islamic finance has long been a subject of study and observation, it is largely unknown. In very general terms, Islamic finance poses two problems: on the one hand, the establishment in Italy of Islamic banks, i.e. operating exclusively in accordance with the precepts of the *Shari'ah* (the code of moral and religious laws with which Islamic financial products must comply), or conventional bank branches specialised in the offer of *Shari'ah* compliant financial products, or still of "Islamic windows ", i.e. ad hoc units within conventional banks offering Islamic

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financial products. Supervision, stability, risk and liquidity management, accounting harmonisation etc., not to mention the European dimension of the single market of financial services allowing the Islamic banks located in other European countries to offer services in Italy, benefiting from the European passport, become relevant issues. The second problem concerns contracts and tax law, and can be approached from three different angles. First of all, the utilisation in Italy of non-conventional *Shari'ah*- compliant contracts, having no particular regulation in our system, which can get through the examination of lawfulness of Article 1322 of the Italian Civil Code only in that aimed at achieving interests deserving protection according to the law. The second approach concerns the enhancement of existing contractual figures provided by our legal system, specifically those with a broadly profit participation cause, such as partnership (Article 2549 Italian Civil Code), investment financial instruments (Article 2346, sixth paragraph of the Italian Civil Code), and assets and loans for a specific business (Article 2447-bis et sequitur) whose utilization in compliance with the principles of the *Shari'ah* will also need to be verified each time in relation to each transaction. The last approach is the ad hoc regulatory intervention that creates, as in other European countries, the legal and tax conditions for the assertion of Islamic finance products. In this sense, for example, in recent interventions on the regulation of the so-called minibonds, finally contained in the Italian Law Decree Destinazione Italia (Destination Italy) probably one could have been more daring, making better use of the variable element of the remuneration of the participation bonds, so as to allow the various funds already established or being established for investing in mini bonds to attract capital also from investors who wish to follow the dictates of the *Shari'ah.* The fund intending to operate according to these principles must in fact not have in the portfolio financial instruments for which a fixed or determinable interest is paid.

Source: MF - Milano Finanza 20/02/2014

Muhammad Ayub

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His encyclopedic work, "Understanding Islamic Finance" published by John Wiley & Sons in October, 2007 is serving as a text book on the subject and as a guide for researchers, financial engineers and practitioners.

Interest, Mark up and Time Value of Money

By Muhammad Ayub

In his article "The debate over 'mark-up'" Dr Aqdas Ali Kazmi raises a question: "Does the Islamic Shariah regard mark-up, or a similar system, consistent with its basic precepts and principles?"

He has discussed stance of Islamic jurists on mark-up during the past two to three decades and drawn the conclusion: "In its operations, structure and use, mark-up resembles interest.... if the Shariah accepts mark-up as valid, it is left with no basis to reject interest.... Shariah jurists cannot reject interest if they accept 'mark-up'".

He has quoted from the Report of Pakistan's Council of Islamic Ideology (June 1980) that the mark-up mode should not be used as a back door for allowing interest into the banking and financial system. The main thrust of this article is to explain Shariah position of the difference between cash and credit prices of a commodity and the possible modus operandi of time valuation according to the precepts of the Shariah. The steps taken by the State Bank of Pakistan for maintaining the purity of Bai Murabaha are also given in the end.

With regard to the credit trade, there had been some difference of opinion among the jurists on the Shariah position of the difference in cash and credit prices of a commodity.

Notwithstanding this difference, there is almost a consensus among the Shariah scholars that credit price of a commodity can genuinely be more than its cash price provided one price is settled before separation of the parties.

Accordingly, the Islamic Fiqh Academy of the OIC and Shariah Boards of all Islamic banks approve the legality of this difference. This is tantamount to the acceptance of time value in the pricing of goods. What is prohibited is any addition to the price once mutually agreed because of any delay in its payment. This is because the commodity once sold, even on credit, belongs to the purchaser on a permanent basis and the seller has no right to re-price a commodity that he has sold and which does not belong to him.

According to many jurists this aspect is approved by the Nass (clear text of the Shariah).

The Holy Quran has reported non-believers saying, "The sale is very similar to Riba."

Their objection was that they increase the price of commodity in the original transaction of sale because of its being based on deferred payment and it is treated as a valid sale.

But if they add to the due amount after the maturity date and the debtor is not

able to pay, it is termed as Riba, while the increase in both cases is similar. This argument has been specifically mentioned by the famous exegetist Ibn-Abi-Hatim (d. 327 AH) (Tafseer, 1999, Vol. 2, p. 545).

The Holy Quran's reply to the above thinking of the non-believers is that "Allah has permitted trading, and prohibited Riba". Allamah Sayyuti and Ibne Jarir Tabari have reported the similar situation of Riba involvement in which a person sold any commodity on credit; when the payment was due and the purchaser could not repay that, the price was enhanced and the time for payment extended (Sayyuti, Lubaab al Nuqool: 1423 and Tabari, Jami al Bayan, Vol. 6, p. 8).

The great Muhaddith Tirmidhi has reported that the Holy Prophet (pbuh) forbade two sales in one contract. Jurists have explained it to mean that a person asks someone, 'I sell this cloth on cash for ten and on credit for 20 (dirhams)' and at separation, one price is not settled. If one of the two prices is settled, it is not prohibited (Tirmidhi, 1988, No. 1254).

Tohfatul Ahwazi, Sharah Jam'i al Tirmidhi, explains that if a seller says that he sells the cloth for 10 on cash and 20 on credit and the buyer accepts any of the two prices; or if a buyer says that he purchases for 20 on credit or the parties separate on any of the prices, the sale will be valid (vol. 2, p. 236).

Shukani explains the above Hadith of the Holy Prophet by concluding that if the purchaser in such a situation says, "I accepted for 1000 on cash", or "for 2000 on credit", it would be all right. He adds that 'Illah (effective cause) for the prohibition of two sales in one is non-fixity of the price (Nail al Awtar, Vol. 5, p. 12).

Shah Waliullah in Muaswwa, Sharah Al Muwatta, writes that if the parties separate after settlement on one price, the contract is valid and there is no difference of opinion in this regard (Al-Musawwa, vol. 2, Pp. 28, 29). Among the scholars of the present age, the late Shaikh Abdullah ibn Baz, who was the most honoured Grand Mufti of Saudi Arabia, permitted the installments sale wherein the credit price could be higher than the cash price (Abdullah ibn Baz, Fatawa, Urdu translation, KSA, 1995, P.142).

Jurists allow the difference between cash and credit prices of a commodity considering it a genuine market practice. It is quite natural that in the market credit price of a commodity is more than its cash price at a point of time while in contracts like Salam (the mode of future trade allowed by the Holy Prophet) the future price will be less than the cash price.

In the words of eminent Hanafi jurist Sarakhsi, "Selling on credit is an absolute feature of trade.... We hold that selling for credit is part of the practice of merchants, and that it is the most conducive means for the achievement of the investor's goal, which is profit.

And in most cases, profit can only be achieved by selling for credit and not selling for cash. He further observes, "A thing is sold on credit for a larger sum than it would be sold for cash" (Al Mabsut, Vol.22, P. 45).

The comments of Abraham L. Udovitch on the views expressed by Sarakhsi are worth mentioning, "This statement makes clear as to why there was a greater profit to be derived from credit transactions..." The difference in price between a credit and cash sale also helps explain why the prohibition against usury, to the extent that it was observed, did not exercise any crippling restriction on the conduct of commerce... (Udovitch, 1970,p.80).

Islamic economics has the genuine provision of converting money into assets on the basis of which one can measure its utility. While it concedes the concept of time value of money to the extent of pricing in credit sale, it does not uphold generating rent to the capital as interest does in credits and advances leading to a rentier class in society.

As per rules of the Shariah, the aspect which matters is the conversion of Rs 1000, for example, into an asset in which case that Rs 1000 asset may be worth more or less in future leading to profit or loss. This conversion into assets is subject to well articulated rules governing profit/loss sharing, trading and leasing.

The concept of time value of money in the context of Shariah is also established fr om the fact that Shariah prohibits mutual exchange of gold, silver or monetary values except when it is done simultaneously. This is because a person can take benefit by use of a currency which he has received while he has not given its counter value from which the other party could take the benefit.

It further transpires that time valuation is possible only in business and trade of goods and not in exchange of monetary values and loans or debts. Loaning is considered in Shariah as a virtuous act from which one cannot take any benefit. Therefore, no time value can be added to the principal of a loan, or a debt after it is created or the liability of the purchaser stipulated.

There should be no confusion in this regard about interest vis-a-vis the concept of rent in Ijarah (leasing). It might be argued, for example, that as per approved Shariah principles, predetermined rent includes a time-value of money,

therefore, a predetermined time value of money in loans/ debts should also be permitted by analogy. This argument does not have any substantive basis. The rent in leasing is calculated on the basis of capacity of the asset to give usufruct, which is in principle uncertain. Hence, it remains uncertain how much time-value of money is actually realized until the asset has completed its economic life. Lessor, as owner of the leased assets, is also the owner of risk and reward of that asset. Further, anything which cannot be used without consuming its corpus cannot be leased out like money, eatables, fuel, etc.

The above discussion leads to an important conclusion that while time-value of money is acceptable in respect of the pricing of assets and their usufruct, it is not acceptable with regard to any addition to the principal of loans or debts. Valuation of credit period based on value of the goods or their usufruct is different from the conventional concepts of 'opportunity cost' or the 'time value'. As such, "mark-up" is permissible provided Shariah rules relating to trade or leasing are adhered to, but interest is prohibited due to being increase over any loan or debt.

On the basis of the above rationale, an overwhelming majority of the Islamic economists believe that economic agents in an Islamic economy will have positive time preference and there will be indicators available in the economy to approximate the rates of their time preferences generally determined by the forces of demand and supply. There is no justification to assume zero rate of time preference in an Islamic economy as is done in a number of studies on investment behavior in Islamic perspective.

Having said that, the permission of charging 'mark-up' in Murabaha is subject to fulfillment of trading rules and conditions set out by the Shariah for such transactions. It goes without saying that the mark-up technique, or for that matter any Islamic modes, should not be used as a back door for allowing interest. The State Bank as a regulator is in the process of designing a framework to ensure compliance of Shariah principles relating to Islamic modes of financing.

State Bank of Pakistan has received comments from bankers, Shariah scholars, economists, educational institutions, business community, etc on guidelines containing Shariah Essentials and Model Agreements of various modes of financing. As and when these guidelines are finalized and approved by the Shariah Board, the same would serve as the basis of the regulatory framework of Islamic banking in the country.

Similarly, the State Bank of Pakistan is the only central bank in the world that has so far planned Shariah compliance audit of Islamic banks/branches. Let's hope that with these steps Islamic banks in Pakistan would be doing Murabaha in line with its true spirit.

The writer is senior joint director in the Islamic banking department of the State Bank of Pakistan. Views expressed in the article are of the writer's and not necessarily of the State Bank.

Integrating Waqf for Realising the Social Goals of Islamic Finance

By Professor Habib Ahmed

Waqf and Islamic finance are in some ways very complimentary concepts. When Islamic finance was first mooted, it was thought to be part of an Islamic economy that would fulfil the goals of Shari'ah, including both legal and social goals, but many observers feel that this has not been the case.

Waqf historically has played a very important role in realising socio-economic welfare goals, but also growth in economies by acting as a third sector. In the past governments typically did not have a social and welfare role by, for example, providing education and healthcare services. In traditional Muslim societies waqf performed this role and it did so very well. In contemporary society waqf has become stagnant as a concept and also in practice.

By contrast, when we look at more developed economies today we see that the third sector has become increasingly important. In the UK, for example there is now an Office of the Third Sector. We do not, however, see waqf playing the same sort of role in Muslim societies.

The Basic Concepts of Waqf

Waqf shares many of the same characteristics of a trust and indeed some Western scholars say that the concept of a trust is derived from waqf. Similar to the concept of a trust, waqf has a founder who donates some assets for a benevolent purpose. This is done through a waqf deed, which is basically the constitution for the governance of the waqf. The deed states the objectives of the waqf; how the resources will be distributed and lays out management procedures. Traditionally a waqf would have a manager, who would usually come from the family of the person setting up the waqf and the deed would state how managers should be appointed.

A waqf has to have a benevolent objective, but that is a very broad ranging objective, so, historically, waqf have been created for a whole range of purposes. Waqf are usually perpetual, but they can be temporary, which was verified recently when the Islamic Fiqh Academy put forward a resolution that makes temporary waqf permissible. There can also be different types of waqf; they can be for public or philanthropic purposes, for family or they can be mixed.

Habib Ahmed

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A Brief History of Waqf

The first waqf was a religious waqf, which was for the Al-Masjid al-Nabaw in Medina created by the Prophet (pbuh), but historically most waqf were for social purposes, everything from education and healthcare through animal welfare to the provision of public utilities. Waqf have undoubtedly made a major contribution to the great Muslim societies of the past, but in recent times the notion of waqf has been somewhat corrupted and the social role has diminished.

The Current Status of Waqf

For a variety of reasons waqf today has become a stagnant institution. Most people do not even know about the history of waqf and the important social role they played and it is no longer performing that socio-economic role. The problem is that waqf are set up in perpetuity and so in many Muslim countries there are waqf assets, mainly properties, which are being completely under-utilised; they are no longer being used for social purposes and they cannot be used for private purposes. The result is that many waqf properties have been lost.

Waqf is not mentioned specifically in the Qur'an or Sunnah; rather it is predominantly derived from fiqh and therefore open to ijtihad. Interestingly, a 2009 Islamic Fiqh Academy resolution made waqf very flexible, breaking away from many of the traditional notions of waqf. For example, the resolution declared that waqf assets can include not just immovable properties, but also sukuk and equities.

Integration Between the Islamic Financial Sector and Waqf

There were a variety of ways in which the Islamic financial sector and waqf could be integrated. The first is for the Islamic financial sector itself to promote the development of waqf by financing waqf properties. In many Muslim countries waqf properties are in prime locations, but, because they have not been developed, the income from them is very small or even non-existent. The other approach is for the Islamic financial sector to offer its management services to manage the waqf properties.

The nature of waqf itself means, however, that there are special considerations in relation to what can be done in terms of financing. When a property is given away as waqf, there is no owner as such; the scholars say it as though the ownership belongs to God himself. Given that fact, it cannot be used as collateral and it cannot be sold.

One solution is to finance the waqf properties directly, but unfortunately most Islamic banks are not doing that. The Islamic Development Bank (IDB), however, has a S50million waqf property investment fund with the sole purpose of investing in waqf properties in IDB'member countries.

The other approach to integrating Islamic finance and waqf is for Islamic financial institutions to go into waqf management. Historically, one of the problems that caused many waqf to degenerate was mismanagement and that is one of the reasons why governments stepped in, although this tended to cause more problems, rather than providing a real solution. The trust management corporations, mirroring the conventional finance sector, could be the answer. Such organisations would offer continuity of management, professional expertise and objectivity.

There are two major ways to provide these sorts of services in conventional finance banks have specialist trust departments and there are independent trust management companies. One example of a bank-based trust management operation in the Islamic finance sector was unfortunately a failure. In around 2006 Dubai Islamic Bank and the Dubai Finance Centre (DFC) came together to form a waqf services company to manage waqf properties, but after two years they had to close, because they could not generate sufficient business. Another example, this time an independent trust management company in Malaysia, AmanahRaya, has been more successful. They do not, however, manage waqf yet. The problem in Malaysia is that if someone creates a waqf, the government basically takes over, but if you create a trust then it can be managed by an organisation such as AmanahRaya.

Waqf-Based Institutions

Another approach is to use waqf in the financial sector. This can be done in three ways – waqf-based microfinance institutions; the use of waqf to guarantee small and micro enterprises and waqf-based takaful, particularly micro takaful with a social orientation.

Waqf-based financial institutions are not new; historically they have been used to finance the poor and needy. There were examples of cash waqf in Turkey and in Iran today there are still qard hasan funds, which started as waqf funds and have become very large.

Bringing waqf to microfinance institutions can be done in three ways. Firstly the cash realized from a waqf fund can be invested and the returns used for microfinance, but the returns are likely to be quite small and therefore the money available for investments will be correspondingly small. An alternative is to use the cash realized to finance projects and businesses in the form of interest-free loans. The third approach, is to use waqf funds as capital to initiate microfinance institutions and really grow this element of the Islamic finance sector, because Islamic banks, with a few

notable exceptions, are not providing microfinance.

The fiqh ruling on waqf guarantees is that these should be given free of charge. Today, however, many Islamic financial institutions have fatwa that allow them to make a charge for providing guarantees.

Islamic financial institutions are in general wary of lending to small and micro enterprises, because the risks are higher. This is usually resolved by governments coming in as guarantors, but I believe that waqf-based institutions could fulfil that role.

Finally, there is waqf-based takaful, which exists today in Pakistan. The logic is that waqf-based takaful is less controversial than other prevalent forms of takaful. It is also possible that it would allow takaful to be spread more widely at the microenterprise level.

In waqf-based takaful participants contribute to a waqf fund and any surplus is shared between the shareholders of the takaful operator and the waqf fund.

Conclusion

Historically waqf has played a very important role in providing socio-economic services. In many countries today, however, waqf is not being used productively, but we believe that the institution can be revived and integrated with the Islamic financial sector. If it were revived, it could provide valuable services to small and micro enterprises, currently not well serviced by Islamic financial institutions.

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A Perspective of Justice in Islâm

By Ibrâhîm Gabriele Iungo

The notion of “Justice” can't properly be regarded as a particular aspect or “topic” within Islamic doctrine: moreover, it's the same essence of Islamic tradition, in its role as ultimate criterion for a human existence consonant with the divine Order. Therefore, it is the same notion of “Justice” to define overall the traditional Islamic doctrine, his *orthopraxis* and jurisprudence. Knowledge (*´ilm*) and deed (*´amal*), doctrine and ritual, comprehension (*fiqh*) and action: the essence of Islâm is a certain faith and a life consistent with it, called upon to be “just” as much as in its intellectual understanding and in its daily-life practice, as part of our social responsibilities. Sufyân ibn ´Abdillah said to the Messenger of Allâh (ﷺ): «Tell me something about Islâm which I can ask of no one but you». He answered (ﷺ): «Say: “I believe in Allâh” - and then be steadfast», resolute in Justice and rectitude (Reported by Muslim).

God the Almighty placed the Justice as archetypal measure of the creation. He (ﷻ) says in the Qur'ân: «*He erected heaven and established the balance*» (55:7). The right fit is what was set from the beginning of creation, what characterizes it throughout its duration, and what will determine the final outcome: «*On that Day, the scale* [of Justice] *shall be established: those whose scale will be heavy will prosper, and those whose scale will be light will find their souls in perdition for that they wrongfully treated our Signs*» (6:8-9). On the universal path that leads from the «establishment of the balance» to the weighing of the deeds of the creatures, Justice is the continuous thread and the hallmark of creation; Prophets and Messengers were sent just to indicate to the people the path of the Justice, calling them to it through a sound knowledge of the Almighty Creator (ﷻ), warning about their forgetfulness and their abandonment, urging to testimony and persevere, even in front of the blunt refusal of the majority of mankind. Testimony, *shahâdah* - similar to the greek *μάρτυς*, *martyr* - is thus the noble vocation of the consistent believer, in front of the tragedy of iniquity.

We can try to identify three key terms, to gain a closest introductory look on the issue.

The first one is the term “*Sharî´ah*”, one of the best known and most misunderstood terms of this era - due to a misunderstanding as serious as fraught with consequences. Generally translated as “*law*”, it means rather “*norm*” or “*measure*”. Its etymology refers to the caravan routes that beat to find water, during the desert crossings - a physical path to the water, which is equivalent to a symbolic path to the Source of sustenance and life. Moreover, the term does not refer linguistically to wells, but to surface waters: still, the symbolic representation

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of the visible that refers to the Invisible, as well as what is superficial refers to what is in depth. In the light of this perspective should be understood the Islamic precepts: they are not only external works and gestures, but rather *symbols* to be implemented, with a deep meaning to be accomplished.

The "heart" of *Sharî´ah* - or rather its essential method - is the ethical commandment of ordering the good and fighting the evil. In the Arabic language, the "good" is indicated by the term "*ma´rûf*", term whose etymology refers to "*ma´rifah*", knowledge. Namely: ethical practice derives directly from spiritual understanding; it is based on a "vertical" bond with the Divine, as suggested by the traditional saying: «*For every right there is a truth*» (*li-kulli ḥaqq ḥaqîqah*). If we lost this "trascendental" dimension, we fall into mere voluntarism, that is unrelated to any genuine spiritual orientation, and devoid of any firm existential anchorage. That's the source of all tragedy.

The second one is the term "*Wasaṭîyyah*", "*equity*"; Allâh (ﷻ) says: «*And thus have We willed you to be a community of the middle way* (ummah wasaṭâ)*, so that* [with your lives] *you might bear witness to the truth before all mankind, and that the Apostle might bear witness to it before you*» (2:143). According to an Arab saying, «*The best of things is their middle*» (*khayr al-umûri awsâṭu-hâ*) or - in other words - *in medio stat virtus*. This is certainly not an istance of mere "moderatism" - as it is said in Revelation 3,16: «*So, because you are lukewarm — neither hot nor cold — I am about to spit you out of my mouth*» - but the statement of the excellence of equity.

For the Muslim believer, equity and balance are summarized in the figure of the Prophet Muhammad (ﷺ) who models all of the aspects of traditional Islamic doctrine. He (ﷺ) is the Seal (*khatm) of all previous Prophets: he* summarizes their qualities, and he is the excellent example of their best characteristics. Furthermore, he is not an abstract reference, or a merely historical figure, but rather a living spiritual presence, through the continuous practice of his personal example and the uninterrupted transmission of his teaching. In fact, the whole Islamic doctrine - starting from the Qur'ân and the authentic collections of the prophetic sayings (*aḥadîth*) - is a continuous retransmission without disruption of his teaching and his manners (ﷺ), so that for example the Qur'ân recited today by any Muslim reproduces exactly the reading taught by the Prophet (ﷺ), not only in the content, but also in the form of expression and intonation. Similarly, he (ﷺ) lives in discipleship observed by believers, who vivify in their lives the prophetic example (*sunnah), in the rituals of their daily existence, "consacrated" in the light of his imitatio - to the point that it's like "if we saw him with our own eyes".*

We can thus understand how equity is not at all an abstract, rationalistic "moral duty", but rather the deed consistent with the prophetic model, perfect example of fairness and balance, firmly based on divine Revelation and positively open to a proper relationship with the divine Principle.

Finally, the third term is "*Khalîfah", "caliph" or "vicar" - which does not represent firstly a political term, but instead consists in a description of the proper function of every human creature. Allâh the* Almighty (ﷻ) *says: «Behold thy Lord said to the angels: "I will create a vicegerent (khalîfah) on earth". They said: "Wilt thou place therein one who will make mischief therein and shed blood? Whilst we do celebrate Thy praises and glorify Thy holy (name)?". He said: "I know what ye know not"» (2:30). Our father Adam was designated as the "vicar of God on earth" (khalîfatu-Llâhi fî l-ard) - and through his loins, all mankind has been tasked with this responsibility. That's why the call (da´wah) of Islâm is addressed to all humanity, without distinction of sex or race, to restore the "original nature" (fiṭrah) of every human creature, that is naturally oriented to the worship of the only divine Principle and to the practice of Justice, which is the application of its ancestral "caliphal" responsibility. Therefore, it's evident how the "caliphal" dimension of the human nature concerns ultimately every human being. Moreover, it should be clear that the "Caliphate" (khilâfah) is only secondarily and - so to speak - accidentally, a particular form of political government: it is firstly an appeal to the re-establishment of an "inner order", on which it is then possible to establish, by the Grace of God, a "just" and peaceful social order. Any violent and irreverent attempt that try to start from the exterior and from the political, to rectify the inner and the spiritual is a sign of these times, which should be corrected and rectified.*

The political state of the societies can only be righted by righting the state of knowledge: that is the root, and the rest is branch. If the root is unwell, pumping fruits with syringes to ripen them is an absurd futility. Our responsibility is to return to the knowledge its centrality in all aspects of our lives, so that we can fulfill our "*caliphal" duties in this life (dunyâ) - and this must be achieved first and foremost in our hearts, so that they are naturally oriented with love and responsibility towards God, and with justice and kindness towards his creatures.*

Halal Soap

By Muhammad Zubair Mughal

The relation between soap and human is as old as the history of culture. Soap has always been the part of civilized society in different shapes either in the shape of Soil collection or mixture of tree leaves and vegetables or mixture of ash and oils while, presently, it comes up with the unique blend of various chemical components, as it is known as liquid soap, beauty soap, toilet soaps and antibacterial soaps etc which is the dire need of each house. As per a careful estimate, about 6 billion people of the world use soap daily and this number is prominently increasing day by day.

But current chemical components and scientific developments have raised differnt questions about the Halal authenticity of soap and have evidently proved the involvement of non Halal ingredients i.e. Tallow extracted from the fat of swine, chemical from the haram animals' flow "Satiric Acid" which is obtained from Lards and all this mixture and blending have distinguished between the division of Halal and haram. While in Islam the matter of Halal and Haram is not only confined to foods rather it is also applied on services (Islamic Banking, Islamic mode of businesses and Islamic Finance etc), clothes and tangible items such as Cosmetics, Soap and Paint etc. When man enters in the category of impurity by touching some haram animals and it becomes mandatory to have shower (Ghusal), then now would it be justified to take bath while using the soaps which is produced with chemicals from the ingredients obtained from same animals? Will his worship be accepted after using that soap?

Hence, it is needed that we should discriminate Halal and Haram in tangible (consumable) items along with food and services. We buy and adopt with joy the leather made imported items such as shoes and hand bags imported from Italy and other countries but do we ever think of the ingredients used in those products and the skin of the animal which was used in those products? Whether the Halal animals are utilized in those countries? If "No" then which animal's skin was used as leather? Which chemicals are used in dying processing of towel that we use to clean the face. Is it obtained from swine's Fat? Which chemicals are used in our paint industry etc? These are the matters of deep concentration that I leave on the readers who need to make the efforts to avoid haram a part of our life. The prime objective of this piece of writing is not to put the Muslims into the fear rather to highlight the issues caused by latest chemical evolutions. If we analyze the current

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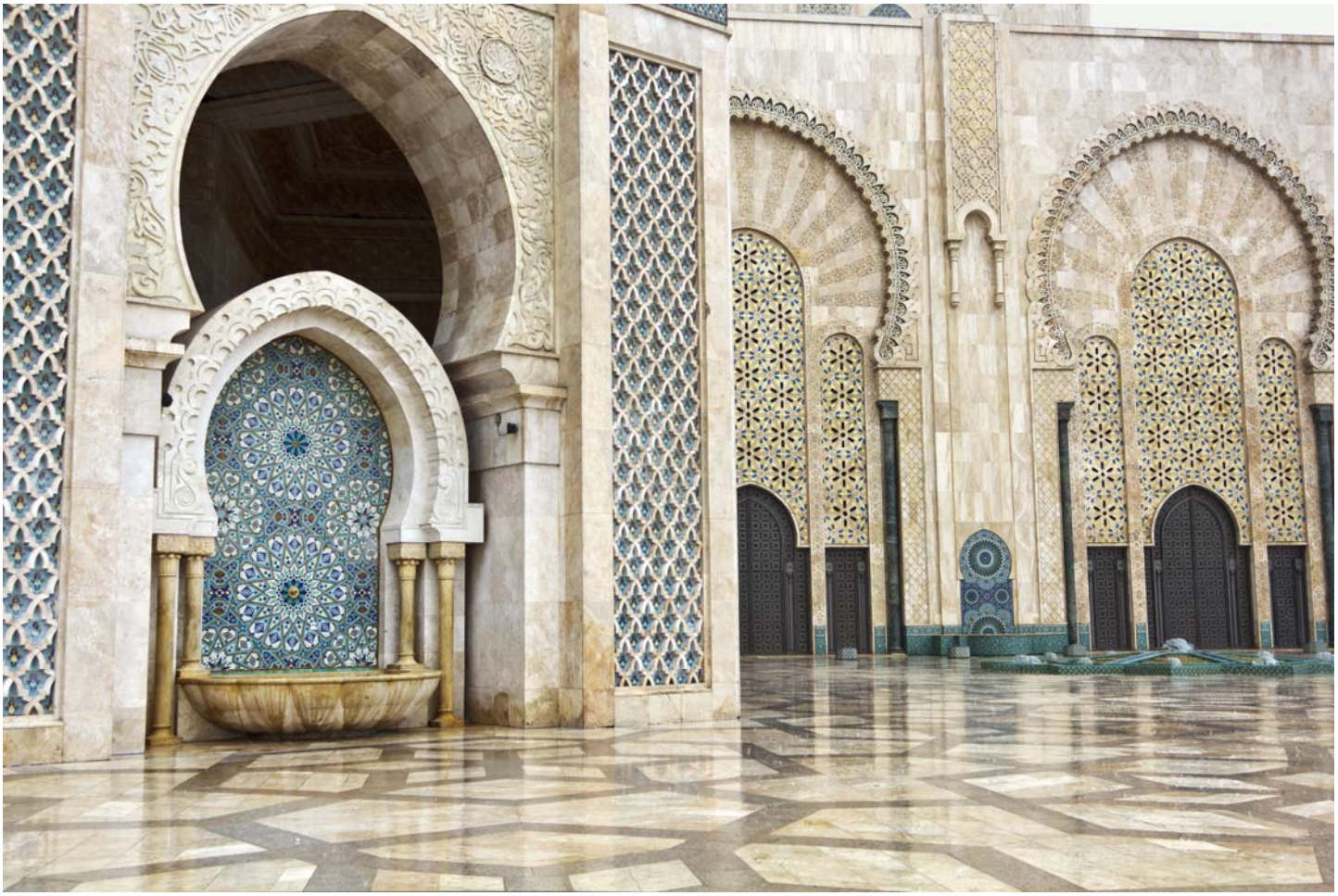

volume of cosmetics industry globally which is about US $ 335 billion but share of Halal cosmetics is US $ 13 billion while our, Muslim, population is about 1.6 billion which is the 26% of whole world population, so, as per these figures, non-Halal cosmetics have more consumption in Muslim countries and the main reason behind it is the lack of awareness and no discrimination between Halal and haram in material items. May Allah (Subhana wa'a Taala'a) forgive us for the sins caused by lack of awareness and give us enough strength to avoid them in future (Aameen).

Halal Research Council (HRC), keeping in view the social, religious and professional responsibilities, inaugurated a specialized department for state of the art research in Soaps, Cosmetics, Dyeing and Paint Chemical to resolve the problems in these industries through in depth research to give a clean and purified society to the Muslim world.

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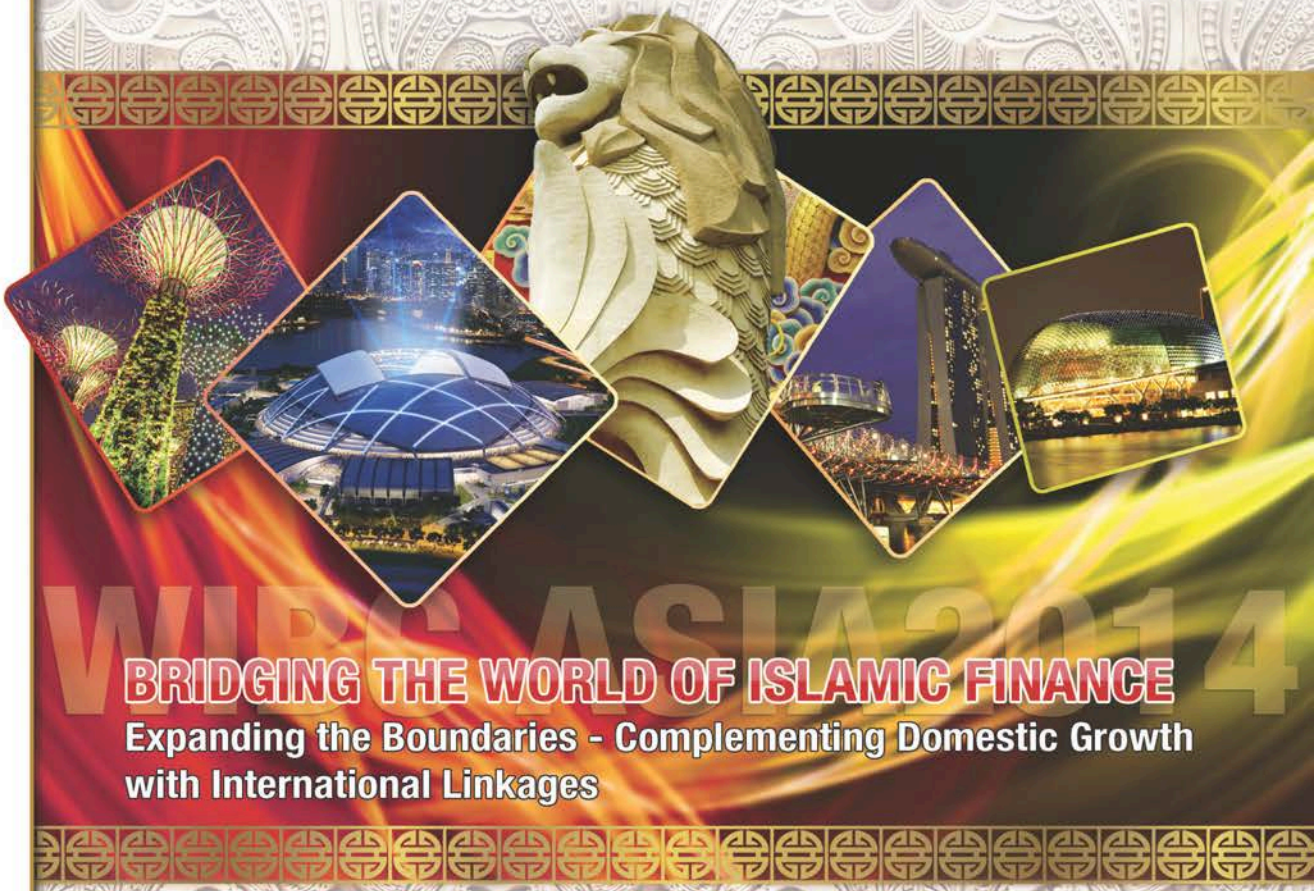

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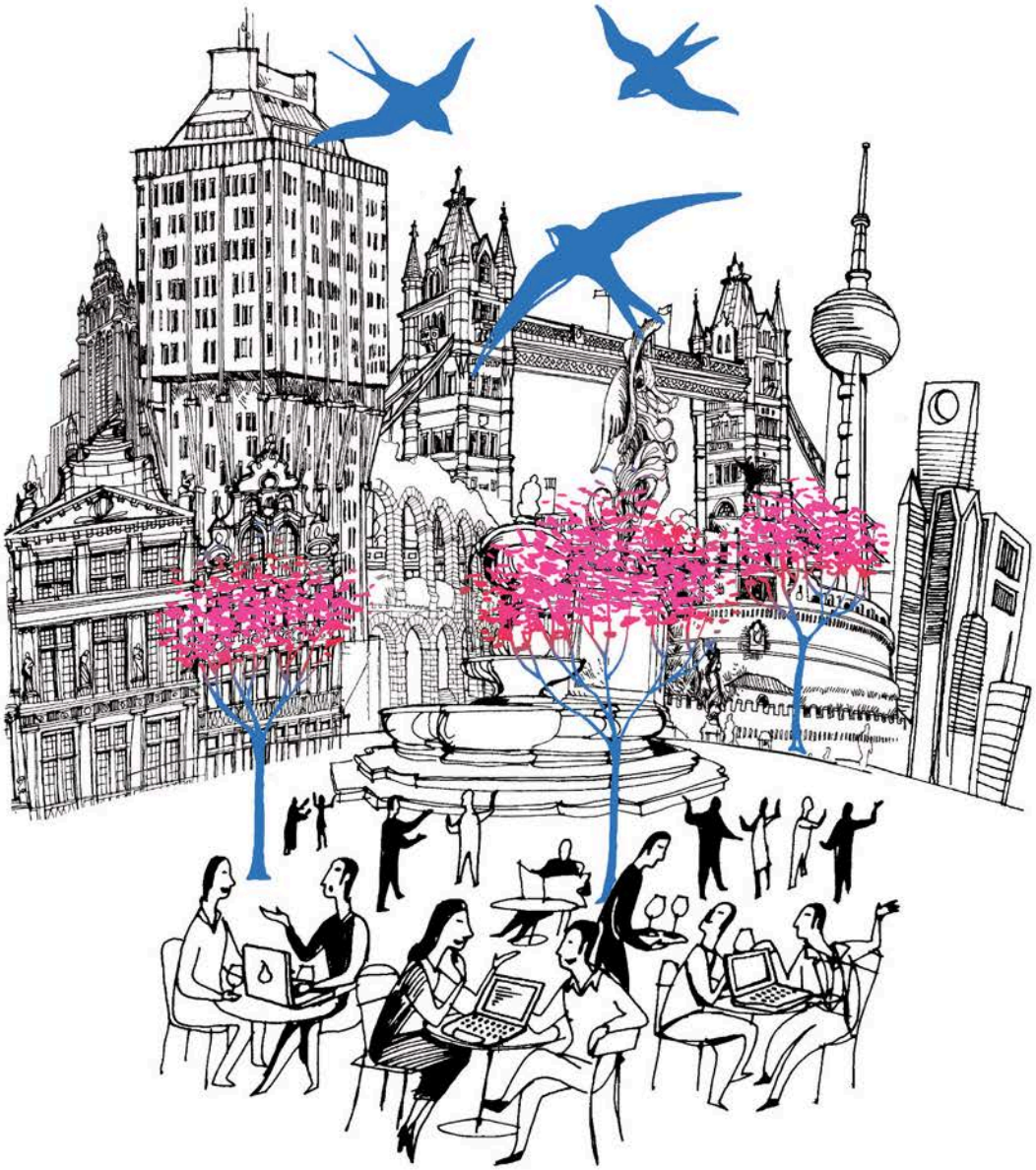

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