Islamic Principles Governing International Trade Financing Instruments: A Study of the Morabaha in English Law

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I. INTRODUCTION

The past years have seen a clear and incontrovertible rise in the use of international financial and commercial instruments expressed to be governed by Islamic principles. Banks and other commercial entities in

1 Such instruments might include investment contracts, their associated guarantees, general financing agreements, suretyship, franchise agreements, commercial agency agreements, Islamic letters of credit, Islamic insurance agreements (“takaful”), etc. There is also no distinction made between agreements involving states as parties, the criterion being the provision, and the receipt of commercial or financial services.

2 This article will not go into the intricacies of the debate on the how these Islamic forms of commerce/finance are to be structured and applied. As a general preface, however, most Islamic scholars agree that the premise of Islamic finance lies in the abrogation of interest (riba) and unpredictability (gharar). Morabaha, ijarah, modarabah and musharakah are common forms of Islamic commercial or financial instruments which avoid riba and gharar. Morabaha is usually described as ‘cost-plus financing’ and frequently appears as a form of trade finance using letters of credit. It involves the sale of goods on a deferred basis. The goods are delivered immediately and the price to be paid will include a mutually agreed margin of profit payable to the seller. In this contract, the market cost price (the true cost) is shared with the buyer at the time of concluding the sale. Ijarah is a form of leasing whereby a known benefit (usufruct) associated with the asset is sold for a payment. In the course of this sale of usufruct, ownership of the asset is not transferred. Instead, the bank maintains ownership of the asset. The contract may allow the bank either to take title of the asset at the
Islamic and non-Islamic countries are increasingly aware of the commercial need to offer services which are specifically tailored to meet this sector of the international market. Disputes over the interpretation and application of such instruments invariably arise. English courts are not insulated from such disputes, given that the City of London is at the forefront of many international commercial and financial dealings. As a matter of law, the question of what law or legal principles should govern the instrument or contract must necessarily be determined. That was indeed the case in *Shamil Bank of Bahrain EC v. Beximco Pharmaceuticals Limited.*

This article uses the *Shamil Bank* case to explore the issue of how compliance with Islamic principles might best be achieved in a financing agreement governed by English law. In particular, it discusses at some length how the author views that the incorporation of Islamic principles might be best achieved, in English law, by means of the proper construction of the contract. Closely allied to that issue is an examination of the English Court of Appeal’s approach to the issue of incorporation of Islamic principles into the financing agreement.

*Shamil Bank* also raises the issue of whether parties could choose Islamic law, as a generic and non-country specific system of law, to serve as the applicable or proper law of the commercial transaction. This area of law is primarily governed by the Rome Convention, ("the Convention"), as end of the lease term or to sell the asset to the customer at the end of the lease period. *modarabah* works on the basis that a *mudarib* or entrepreneur will provide management expertise as capital. The investor is known as the *rabb al-mal* who bears all losses of invested assets. The share of expected future profits between the *mudarib(s)* and the investor(s) is agreed at the outset in any ratio mutually agreed to by the parties involved. With the *musharakah*, all the parties are involved in a partnership arrangement and must contribute funds, but they will all have the right to exercise executive powers in the venture. See generally [Dinar Standard: Business Strategies for the Muslim World, http://www.dinarstandard.com (last visited Oct. 10, 2006)] for an introduction to Islamic business concepts. See also Rodney Wilson, *The Evolution of the Islamic Financial System, in ISLAMIC FINANCE: INNOVATION AND GROWTH* 29 (Rifaat Ahmed Abdel Karim & Simon Archer eds., 2002) for a recent analysis of these concepts. For background information on the topic of Islamic Banking, see generally J. Michael Taylor, *Islamic Banking—The Feasibility of Establishing an Islamic Bank in the U.S.,* 40 AM. BUS. L.J. 385 (2003); Humayon Dar & John Presley, *Lack of Profit Loss Sharing in Islamic Banking, 2 Int'l J. ISLAMIC FIN. SERV.* 1 (2000); Goharb Bilal, *Islamic Finance: Alternatives to the Western Model, Fletcher Forum of World Affairs* 145 (1999); Institute of Islamic Banking and Insurance, [http://www.islamic-banking.com (last visited Oct. 10, 2006)]; International Journal of Islamic Financial Services, [http://islamic-finance.net/journals (last visited Oct. 10, 2006)].


incorporated into English law by means of an Act of Parliament, the Contracts (Applicable Law) Act 1990 ("the Act"). The Convention was intended to harmonize the rules relating to the proper law of the contract amongst E.U. Member States. The traditional English common law proper law of contract doctrine has been replaced; the Act, and consequently, the

The United Kingdom signed on to the Rome Convention on December 7, 1981. Although the Rome Convention is mostly a measure of E.U. law, id. art. 2, and indeed requires contracting states to refer any questions of law to the European Court and to decide any such question in accordance with the principles laid down by the European Court, id. art. 3, Article 2 makes it plain that any law specified by the Convention shall be applied whether or not it is the law of a contracting state. Id. art. 2.


6 F. A. Mann commented: "The Act replaces one of the great achievements of the English judiciary during the almost 140 years or so, an achievement which produced an effective private international law of contracts, was recognized and followed in practically the whole world and has not at any time or anywhere led to dissatisfaction or to a demand for reform." The Proper Law of the Contract—an Obituary, 107 L. Q. Rev. 353, 353 (1991). That might, however, be an overly pessimistic view; it might be argued that the tools developed by the common law to help ascertain the applicable or proper law of the contract are, to a large extent, also used by the Rome Convention. In the case of an express choice of law clause, the Rome Convention is not substantially dissimilar to the common law's emphasis on party autonomy. As for the applicable law in the absence of choice, the Rome Convention differs from the common law by providing presumptions to be used. See Rome Convention, supra note 4, art. 4(2). But the foundation for those presumptions is the same—that the aim of the presumptions is to ascertain which country has the closest and real connection with the contract. Indeed, where the presumptions are inapplicable, Article 4(5) requires the court to consider all the circumstances to establish which country has a real connection which is the closest to the contract. Id. art. 4(5). That is not dissimilar to the common law's proper law doctrine. See In re United Rys. of the Havana and Regla Warehouses Ltd., [1960] 2 W.L.R. 969; The Assunzione, [1954] 2 W.L.R. 234. As McClean said in this context, "in other words, the primacy of the test of closest connection is re-asserted. The result may well be that, at least in courts such as those of England which are used to a flexible test, the presumptions will be resorted to only in 'tie-break' situations, and will have little importance in most cases." JOHN DAVID MCCLEAN, MORRIS: THE CONFLICT OF LAWS 263 (J.H.C. Morris ed., Sweet & Maxwell 1993). For examples of cases which apply the Rome Convention test, see Apple Corps v. Apple Computers, [2004] EWHC (Ch) 768, [44]-[68] (Eng.); Armstrong Int'l v. Deutsche Bank Sec. Inc., [2003] All E.R. (D) 195 (Eng.); Marconi Commc'n's Int'l Ltd. v. PT Pan Indon. Bank Ltd., [2004] EWHC (Comm) 129, [18]-[31] (Eng.); Definitely Maybe (Touring) Ltd. v. Marek Lieberberg Konzertagentur GmbH, [2001] 1 W.L.R. 1745, [5]-[15] (Comm) (Eng.) (explaining how the Article 4(5) can displace the presumptions in Article 4(2) in limited circumstances).

Be that as it may, the romanticism of English conflict of laws has finally yielded to written law and with that, one might wonder what Professor Cheshire might make of all these E.U.-induced changes. Professor Cheshire wrote in 1935 that:

Of all the departments of English law, Private International Law offers the freest scope to the mere jurist. . . . It is not overloaded with detailed rules; it has been only lightly touched by the paralyzing hand of the Parliamentary draftsman; it is perhaps the one considerable department in which the formation of a coherent body of law is in course of process; it is, at the moment, fluid not static, elusive not
Convention, applies in England and Wales to all contracts made after April 1, 1991. If Islamic law cannot operate as the applicable law of the contract, what are the legal implications under the Convention for a choice of foreign or English law where the contract has a connection with a country where Islamic principles are applied?

II. THE FACTS OF SHAMIL BANK

The claimant bank had applied for summary judgment against the defendants. The basis of the claim was that the defendants, Beximco, and others, had failed to honor their obligations under a financing agreement made with the bank. The agreement might be generally described as a “Morabaha” agreement, which under Islamic law required that the bank, as seller, to acquire possession of the goods. In turn, the bank would sell the goods to the defendants who would take delivery and make installment payments with the addition of a pre-agreed profit. The contract was essentially a sale between the defendants and the primary sellers, with the bank acting as a financier. Because the imposition of interest, *riba*, is prohibited under Islamic law, the bank needed to step in as a secondary buyer who would pay for the goods and then resell them to the defendants at a profit. The agreement stated that “subject to the principles of the Glorious Sharia, this Agreement shall be governed by and construed in accordance with the laws of England.”

The use of such clauses is not a rare occurrence. Many Islamic financial institutions have a significant presence in the City of London or elsewhere in the European Union or the United States and have full access to international lawyers in those jurisdictions. They see no commercial imprudence in choosing these jurisdictions for litigation purposes. Also, as all parties to a contract are not necessarily Islamic, Islamic financing institutions and traders are adroit to see that international parties to a contract might perceive an English jurisdiction clause as particularly advantageous for the purposes of commercial certainty.

The *Shamil Bank* defendants’ argued that, because of the governing law clause, the agreements were only enforceable if they were valid in the

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7 See supra note 2 (explaining basic background information on Islamic banking and providing general information on sources for further study).


9 A syndicated financing arrangement is one example of a contract that may have both Islamic and non-Islamic parties.
eyes of both English and Sharia law. The defendants alleged that certain parts of the contract were contrary to Sharia law because they were in fact disguised loans requiring the payment of interest, thus rendering the entire contract invalid. If the agreement was invalid for this reason, both the debtors and guarantors would be discharged. In the alternative, the defendants argued that the guarantees had been entered into on the basis of a common mistake as to the validity of the agreements under Sharia law and were therefore of no effect.

The trial judge held that English law was the governing law because there could not be two separate systems of law governing the contract. The trial judge also held that the parties had not chosen Sharia law as the governing law because as a set of religious principles, Sharia law was not the law of a country, and therefore the parties could not have intended the secular English court to resolve matters of religious controversy.

III. THE ROME CONVENTION: NO TWO COMPETING APPLICABLE LAWS

According to the Convention, the first step in determining the applicable contract law is to determine if the parties agreed to a choice of governing law. Party autonomy is the cornerstone of the Convention. Article 3 provides:

(1) A contract shall be governed by the law chosen by the parties. The choice must be express or demonstrated with reasonable certainty by the terms of the contract or the circumstances of the case. By their choice the parties can select the law applicable to the whole or a part of the contract.

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10 Shamil Bank, [2004] EWCA (Civ) 19, [27].
11 Id.
12 The focus of this article will be on the issue of incorporation of Sharia principles, and not on English law rules on common mistakes. On the issue of mistake, however, Lord Steyn of the Court of Appeal held that a common mistake as to the legal consequences of the Morabaha agreements would not qualify as a mistake apt to give rise to a defense because the mistake was not one such as to "render the subject matter of the contract essentially and radically different from the subject matter which the parties believed to exist." Assoc. Japanese Bank Int'l Ltd. v. Crédit du Nord SA, [1989] 1 W.L.R 255, 268. More generally, mutual mistake has been defined as rendering "the thing [contracted for] essentially different from the thing [that] it was believed to be." Great Peace Shipping Ltd. v. Tsavliris Salvage Int'l, [2002] EWCA (Civ) 1407, [47] (quoting Bell v. Lever Brothers Ltd., [1932] A.C. 161, 218 (H.C.) (opinion of Lord Atkin)). For a commentary on Great Peace Shipping Ltd. v. Tsavliris Salvage Int'l, see D.R. Thomas, Contract of Hire in Aid of Salvage—Common Mistake, 9 J. INT'L MAR. L. 25 (2003).
14 Id. [36]-[38].
The parties may at any time agree to subject the contract to a law other than that which previously governed it, whether as a result of an earlier choice under this Article or of other provisions of this Convention. Any variation by the parties of the law to be applied made after the conclusion of the contract shall not prejudice its formal validity under Article 9 or adversely affect the rights of third parties.

Although Article 3(1) does not specifically refer to the law of a specified country, other Articles of the Convention demonstrate that Article 3(1) should be interpreted as choice of law of a definable legal system of a state. For example, Article 2 states that any law specified by the Convention would be applied whether or not it is the law of a Contracting State. Additionally, Article 3(3) states that parties' choice of a foreign law "shall not, where all the other elements relevant to the situation at the time of the choice are connected with one country only, prejudice the application of rules of the law of that country which cannot be derogated from by contract." Such rules are generally known as "mandatory rules." This provision of the Convention anticipates the choice of the law of a foreign country. Furthermore, Article 4 provides that where the

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15 Rome Convention, supra note 4, art. 9 (addressing the rules of formal validity for the contract). The article provides that a contract is formally valid if it satisfies the formal requirements of the applicable law or of the law of the country where it is concluded. Id. art. 9(1). Where the contract is concluded between persons who are in different countries, the contract is formally valid if it satisfies the formal requirements of the applicable law or of the law of one of those countries. Id. art. 9(2). Where the contract is concluded by an agent, the country in which the agent acts is the relevant country for the purposes of subsections 1 and 2 of Article 9. Id. art. 9(3).


17 Rome Convention, supra note 4, art. 2. The Rome Convention is open to signing only by members of the Europen Union. Id. art. 28. Hence, a Contracting State in Article 2 is defined as an E.U. member state which is a signatory of the Convention. Id. art. 2. Courts may consult the Giuliano-Lagarde Report for guidance when interpreting the Rome Convention. Contracts (Applicable Law) Act 1990, c. 36, § 3(3)(a) (U.K.).

18 Rome Convention, supra note 4, art. 3(3) (emphasis added). This section appears to be of limited applicability because it is generally improbable in an international contracting situation that all of the relevant elements associated with the choice of law would be connected with only one country.

19 Id.

20 See LAWRENCE COLLINS, 2 DICEY & MORRIS ON THE CONFLICT OF LAWS 1223
parties had not made an express selection, the contract shall be presumed to be governed by the law of the *country* with which it is most closely connected.\(^{21}\) This implies that the Convention excludes non-country specific sets of rules, such as the *lex mercatoria*, international human rights, international law or *Sharia* law, as possible sources of foreign law.

The 1972 draft of the Convention, which provided that the Convention would only apply "in situations of an international character,"\(^{22}\) is early evidence of the view that the Convention should govern conflicts between the laws of countries, not systems. This limitation was subsequently rejected because of interpretative problems it was likely to cause.\(^{23}\) A clearer statement of the scope of the Convention re-appeared in Article 1(1), which states: "the rules of the Convention shall apply to contractual obligations in any situation involving a choice between the laws of different countries."\(^{24}\) Article 19(1) suggests that "country" includes any territorial unit, whether it is a single state or a mere unit of a larger state, which has its own rules of law in respect of contractual obligations.\(^{25}\) Therefore, the legislative history and text of Article 1(1) supports the proposition that the notion of applicable law is one associated with countries. Therefore, the general scheme of the Convention is that the reference point for the choice

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\(^{21}\) Rome Convention, *supra* note 4, art. 4. There are a number of aids provided for by the Convention on how the country with which the contract has the closest connection might be presumed, for example:

\[\text{[I]t shall be presumed that the contract is most closely connected with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of conclusion of the contract, his habitual residence, or in the case of a body corporate or unincorporate, its central administration. However, if the contract is entered into in the course of that party's trade or profession, that country shall be the country in which the principal place of business is situated or, where under the terms of the contract the performance is to be effected through a place of business other than the principal place of business, the country in which that other place of business is situated.}\]

*Id.* art. 4(2).


\(^{24}\) Rome Convention, *supra* note 4, art. 1(1).

\(^{25}\) *Id.* art. 19.
of law, whether express or presumed, should be a country.

If the Rome Convention restricts contractual choice of law provisions to selection of the law of a particular country, it follows that, as a matter of contract law, the requirements for legal certainty would not generally permit a contract to be subject to two applicable laws. In other words, a flexible choice of law clause, which permits a party to pick one out of two or more possible applicable laws, would fail for want of certainty. Unlike a flexible choice of forum clause which may be enforceable depending on its clarity, a flexible choice of law could not be enforced because a contract must define the governing law right at its inception. The defined governing law gives life to the contract. The forum clause, on the other hand, merely prescribes the place where that contract might be litigated; it does not give succor to the contract like the governing law.

This single applicable law restriction traces its roots to common law, but there is no indication that the Rome Convention diverges from the common law on this point.

Common law itself has always been institutionally distinctive. A common law judge could not apply principles of equitable law until 1876. This institutional distinctiveness supports a conflicts rule that prohibits selective application of two competing proper laws.

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26 The same would also apply because of the requirements for commercial certainty.


28 Examples of flexible choice of law clauses might include: “Chinese law or English law at the defendant’s option” or “Spanish law or English law at the Bank’s option.”

29 The same would also apply because of the requirements for commercial certainty.


31 See generally Supreme Court of Judicature Act, 1873, 36 & 37 Vict., c. 66 (Eng.); see also Supreme Court of Judicature Act, 1875, 38 & 9 Vict. c. 77 (Eng.).

32 The common law has always been flexible enough when transplanted into a colonized environment to admit the application of personal laws and customs distinctive to the local populations. Courts of Judicature in the colonies, from India to the Straits Settlements, were empowered and exhorted to exercise all the jurisdiction of the English courts of law and chancery “as far as circumstances [would] admit.” Saik v. Drashid, [1946] 1 Malayan L.J. 147, 152 (App. Ct. Sept. 13, 1941). With respect to personal laws, Straits Settlements Charter of 1855 allowed the courts of judicature to exercise jurisdiction as an ecclesiastical court “so far as the several religions, manners and customs of the inhabitants will admit.” Roland BraddeIl, BraddeIl’s Law of the Straits Settlements 17 (3rd ed. 1982); Ying v. Chan [1933] 2 Malayan L.J. 301, 304 (Civ. Ct. Selangor July 27, 1933) (quoting same); Abdullah v. Palamai [1935] 1 Malayan L.J. 147 (Civ. Ct. Singapore Apr. 13, 1935)
The proposition that a contract cannot be governed by two competing applicable laws is consistent with the doctrine of severance\(^\text{33}\) described in Article 3(1) of the Convention. Article 3(1) states that the parties may select the law applicable to a subset of the contract or to the entire contract.\(^\text{34}\) The doctrine of severance does not allow a single contractual provision to be subject to two competing laws. Rather, each distinct and severable provision of the contract may be subject to a different set of applicable laws, within the bounds that the resulting contract is not uncertain or absurd. Indeed, the Giuliano-Lagarde Report\(^\text{35}\) anticipates the choice of law problems that severance may cause, and makes it clear that severance should be employed "as seldom as possible" and only "for a part of a contract which is independent and separable, in terms of the contract and not of the dispute."\(^\text{36}\)

(quoting same); Mustan v. Rex [1946] 1 Malayan L.J. 36, 38 (App. Ct. Nov. 3, 1941) (citing same). For an application of the maxim, see e.g., Ong Cheng Neo v. Yeap Cheah Neo (1874–75) L.R. 6 P.C. 381, 393–94 (P.C. 1875) (appeal taken from Sup. Ct. of Straits Settlement). In contrast, in the pre-Empire days, the position was less pragmatic and a distinction was made between Christian and non-Christian territories. Lord Coke, for example, said in Calvin's Case, 7 Co. Rep. 1a, [18a] (1608) reprinted in 77 ENGLISH REPORTS 377, 398 (1932): "If a King conquers a Christian kingdom... he may at his pleasure alter the laws of the kingdom, but until he [does] so, the ancient laws... remain. But if a Christian king should conquer the kingdom of an infidel, and bring them under his subjugation, [then] ipso facto, the laws of the infidels are abrogated, for that they are not only against Christianity but against the law of God and of nature, contained in the Decalogue..." That theory was subsequently expunged by Lord Mansfield, a mercantile court judge, in Campbell v. Hall, Lofft. 655, 716 (1774) reprinted in 98 ENGLISH REPORTS 848 (1932): "Don't quote the distinction [between Christians and non-Christians] for the honour of my Lord Coke." As David Pearl wrote: "By the end of the colonial era, indigenous law was recognized as law proper by all the colonial powers, with the exception of Germany, and as a result, internal conflict of law rules developed to regulate the legal relations of the autochthonous population and the colonials, and of the various sectors of the autochthonous population." \[DAVID PEARL, INTERPERSONAL CONFLICT OF LAWS 26 (1981).\]


\(^{34}\) Rome Convention, \textit{supra} note 4, art. 3(1).


\(^{36}\) Id. An example of a contract containing an index-linking clause is where the index linking clause might be subject to an applicable law different from what applies to the rest of the contract. However, it is thought that such a severance would not cause problems of certainty and is therefore enforceable under Article 3(1). \textit{Id.} at 17.
IV. ANALYSIS OF SHAMIL BANK: A MATTER OF CONSTRUCTION

Given the fact that English law prohibits two competing applicable laws of the contract, and the Rome Convention’s choice of law restriction to the laws of a country, the claimant bank could not argue that Sharia law was the applicable law of the contract in question. The defendants submitted that the governing law clause demonstrated that the parties had intended that an English court should also be cognizant of the principles of Islamic law while applying English law as the applicable law of the contract. In other words, the defendants asserted that it was not repugnant to the conflicts rule to read into the contract a condition precedent that the contract was only enforceable insofar as it is consistent with the principles of Sharia, whose principles amount to legal rules ascertainable and applicable by an English court.

The lower court addressed the issue of whether the governing law clause manifested an intention by the parties to require an English court to adopt Islamic legal principles when applying English law. The lower court held that there was too much uncertainty in the clause to permit such a construction because the “Glorious Sharia,” referred to by the clause, embodied both legal and religious principles, and therefore, the parties could not have intended to expect an English court to apply a set of religious principles whose content is, in many respects, controversial.

On appeal, the defendant-appellants argued that asking an English court to apply English law in harmony with Sharia law when interpreting a contract was neither an unusual request, nor was it outside of the capabilities of the court. Historically, English courts have been able to apply English law alongside a body of codified non-country specific legal rules, such as the Warsaw Convention or the Hague Rules, where there is an incorporation clause such as a paramount clause. The defendant-appellants argued that the governing clause in the contract in the instant case could be analogized to a paramount clause in a carriage contract. The claimant bank had held itself out as an Islamic bank conducting Islamic

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40 Shamil Bank, [2004] EWCA (Civ) 19, [44].
41 See Nea Agrex S.A. v. Baltic Shipping Co., [1976] 1 Q.B. 933, 934 (holding that “the incorporation of the paramount clause into the charter party meant that all the accepted Hague Rules . . . were brought into the charterparty.”) With that ruling, the Court of Appeal overruled the lower court’s finding that a paramount clause was ineffective in incorporating the Hague Rules into a charterparty. Id. at 946.
42 Shamil Bank, [2004] EWCA (Civ) 19, [43].
banking business, and therefore, it was clear that the parties intended to apply relevant Islamic principles to the contract.\textsuperscript{43}

Additionally, the defendant-appellants argued that the lower court’s holding was flawed because of its emphasis on the uncertainties and controversies generally surrounding \textit{Sharia} law.\textsuperscript{44} The defendant-appellants argued that the court is entitled to seek expert evidence on the specific provisions of the legal corpus applicable to the contract in question.\textsuperscript{45} Therefore, the lower court’s concern of being ill-equipped to apply \textit{Sharia} law was overstated.

Finally, the defendant-appellants argued that the lower court erred in holding that the \textit{Sharia} principles relevant to the contract were controversial.\textsuperscript{46} While the defendant-appellants conceded that there are some controversial aspects of \textit{Sharia} law as applied to contracts, \textit{Sharia} law as applied to the contract in question did not present a controversy.\textsuperscript{47} The appellants argued that the proscription of \textit{riba} and the essentials of a valid \textit{Morabaha} agreement were not controversial, and as such, the lower court should have applied the principles in interpreting the contract.\textsuperscript{48}

A. Intent of the Contracting Parties

The Court of Appeal applied principles of contract construction to analyze the defendant-appellant's arguments. The starting point was Lord Wilberforce's dictum in \textit{Reardon Smith Line Limited. v. Yngvar Hansen-Tangen}:

\begin{quote}
In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.\textsuperscript{49}
\end{quote}

After analyzing the transaction, the Court of Appeal viewed the loan

\begin{footnotesize}
\textsuperscript{43} Id. [6]–[9], [43].
\textsuperscript{44} Id. [45].
\textsuperscript{45} Id. (citing Islamic Inv. Co. of the Gulf (Bah.) Ltd. v. Symphony Gems NV, 2001 Folio 1226, slip. op. at 10–12 (EWHC (Comm) Feb. 13, 2002), available at 2002 WL 346969 (no pagination available); also available at http://www.lawtel.com (original court transcript with page numbers)); but see Al-Bassam v. Al-Bassam, [2002] EWHC (Ch) 2281, rev’d on other grounds, [2004] EWCA (Civ) 857 (noting that the court was quite prepared, upon evidence by expert witnesses, to inquire into the intricacies of Islamic law) and Glencore Int’l AG v. Metro Trading Int’l Inc, [2001] 1 Lloyd’s Rep. 284 (same).
\textsuperscript{46} Shamil Bank of Bahr.EC v. Beximco Pharmas. Ltd, [2004] EWCA (Civ) 19, [45].
\textsuperscript{47} Id.
\textsuperscript{48} Id.
\end{footnotesize}
agreements as interest bearing transactions couched and disguised in Morabaha terms, because the defendants intended for the bank to contribute to their working capital, and the goods specified in the agreements were merely a vehicle to swell the working capital. The court noted that:

[N]either side was under any illusion as to the commercial realities of the transactions, namely the provision by the Bank of working capital on terms providing for long term repayment, and both were content ‘to dress the loan transactions up as Morabaha sales . . .’, whilst taking no interest in whether the proper formalities of such a sale or lease were actually complied with . . .

The Court of Appeal naturally leaned towards a contract construction which serves the commercial objective of the contract rather than one which defeats it. The commercial objective was the provision of capital on “conventional” terms couched in Islamic compliant language. The court found the contractual references to Sharia were less than genuine and were instead part of a marketing and public relations enterprise. While the court was careful not to allude to the defendant-appellants’ honor or good faith, it can be inferred that the court was unwilling to carry on the façade and give force to a venture where reliance on Islamic principles was sought for less than honorable reasons. The Court of Appeal took a sound approach to the case, ascertaining the commercial objective of the agreement and then applying a construction, as long as it is not absurd, which promotes that objective.

Although the appellants in Shamil Bank conceded that the contracts in question were actually conventional interest bearing agreements disguised as Morabaha instruments, the case raises the issue of how an English court might analyze a contract when a Morabaha instrument is genuinely intended. Making the distinction between a genuine Morabaha instrument and a standard loan dressed up as a Morabaha is neither easy nor practical. In Shamil Bank, the court found that prior to the lawsuit, the defendant-appellants had no reservations about the agreement on religious grounds or conflicts with Sharia law. As previously noted, the Court of Appeal emphasized the fact that both parties to the contract had “no interest in whether the proper formalities of such a sale or lease were actually

50 Shamil Bank, [2004] EWCA (Civ) 19, [19]–[26]. There were also ancillary contracts in the transaction which took the form of ijarah leases in the case but for our purposes and convenience, it is sufficient that the contract was found to have been dressed as Islamic compliant transactions. Id. [20].

51 Id. [28].

52 Id. [47] (emphasis added).
complied with." On that basis, the Court of Appeal concluded that the transaction was therefore not a genuine Morabaha instrument but a standard loan transaction disguised as a Morabaha agreement. The problem with this approach is that the Court of Appeal, by insisting on a genuine link between the subject matter and the financing institution, had made its own assessment as to what constitutes a genuine Morabaha instrument without reference to Islamic law and practice. Therein lies the essence of the issue—the Morabaha instrument is intended to be a substitute for or an alternative to "conventional" financing, but the Court of Appeal ruling in Shamil Bank may have improperly limited the flexibility of the Morabaha instruments as a form of financing by requiring the financing bank to have a real and substantive link with the subject matter. The Court of Appeal holding in Shamil Bank has clearly defined a Morabaha as a sale transaction, and not as a financing arrangement. The court in Shamil Bank was clearly swayed by the fact that the purpose of the Morabaha arrangement was to provide working capital for the defendants, not to finance the purchase of goods. Nevertheless, the court's emphasis on establishing a genuine link between the Morabaha and the goods in order to determine the commercial object of the Morabaha makes the use of such Islamic financing arrangements less clear not only in the context of choice of law but also in a general commercial or contractual context.

B. Viability of Morabaha Agreements as Financing Instruments

The court's analysis in Shamil Bank might be juxtaposed against the current debate on the viability of the Morabaha as a form of Islamic financing. Some Islamic scholars take the view that the Morabaha mimics the interest-bearing convention financing, because the fixed-profit margin is frequently adjusted based on the interest rate of a particular country (such as the London Inter-Bank Offer Rate, "LIBOR") and is in actuality a simple sale on cost-plus basis. Scholar and retired Justice Mufti Muhammad Taqi Usmani noted the closeness of Morabaha to interest-based financing, stating that "murabaha is a border-line transaction and a slight departure from the prescribed procedure makes it step on the prohibited area of interest-based financing. Therefore, this transaction must be carried out with due diligence and no requirement of Shari'ah should be taken lightly." Other well-respected commentators have criticized Morabaha arrangements as mere window dressing for conventional interest-bearing

53 Id.
55 El-Gamal, supra note 54, at 128 (citing MUHAMMAD TAQI USMANI, AN INTRODUCTION TO ISLAMIC FINANCE 152 (1988)).
financing.\textsuperscript{56} Indeed, there is evidence of some Islamic banks moving away from the \textit{Morabaha} arrangement to \textit{ijarah} leasing.\textsuperscript{57} In \textit{ijarah}, the fixed rate of return is designated as rental payment for the underlying asset.\textsuperscript{58} While the asset must have a legitimate usufruct, (in other words, the goods must be tangible), this requirement is easily satisfied by movable and immovable property assets. The \textit{ijarah} leasing arrangements are not entirely free of characteristics resembling interest-bearing financing, because even in the \textit{ijarah}, the fixed rental return is frequently tied to the interest rate of a particular country such as LIBOR.\textsuperscript{59} If commentators cannot agree on whether \textit{Morabaha} arrangements and \textit{ijarah} leasing are truly something other than interest-bearing financing, it is no wonder why English courts evaluating these contracts have difficulty distinguishing between “window dressing” and the expression of a genuine Islamic compliant instrument.

C. Incorporation Principles and Islamic Law

The Court of Appeal in \textit{Shamil Bank} also addressed the issue of whether an analogy might be drawn from paramount clauses in transport/carriage contracts. The court held that:

The doctrine of incorporation can only sensibly operate where the parties have by the terms of their contract sufficiently identified specific ‘black letter’ provisions of a foreign law or an international code or set of rules apt to be incorporated as \textit{terms of the relevant contract} such as a particular article or articles of the French Civil Code or the Hague Rules.\textsuperscript{60}

The Court of Appeal held that general reference to the “\textit{Glorious Sharia}” in the contract was not sufficient to incorporate it as “terms of the relevant contract.”\textsuperscript{61} The Court of Appeal continued by explaining that “[t]he general reference to principles of \textit{Sharia} afford no reference to, or

\textsuperscript{56} Id.

\textsuperscript{57} The majority of the financing instruments used are still in the \textit{Morabaha} form, but there is evidence that some banks are developing other forms of financing, including the \textit{ijarah} and the \textit{musharakah}. Id. Indeed, regret has been expressed that too many market operators are too conservative in not venturing beyond the \textit{Morabaha}. See Rafi-uddin Shikoh, \textit{Corporate Islamic Finance: The Good News and the Bad News}, \textit{Dinar Standard}, July 20, 2005, http://dinarstandard.com/finance/corporateF071505.htm (last visited Oct. 26, 2006).

\textsuperscript{58} See generally Taylor, \textit{supra} note 2, at 397.

\textsuperscript{59} El-Gamal, \textit{supra} note 54, at 128.


\textsuperscript{61} Id.
identification of, those aspects of Sharia law which are intended to be incorporated into the contract, let alone the terms in which they are framed.”

The Court of Appeal, in addressing the argument that to not give legal effect to the contractual reference to Sharia was to treat the words as mere surplusage, affirmed the lower court’s view that the clause was intended no more than:


to reflect the Islamic religious principles according to which the Bank holds itself out as doing business rather than a system of law intended to ‘trump’ the application of English law as the law to be applied in ascertaining the liability of the parties under the terms of the agreement.

It is difficult to reconcile the Court of Appeal’s holding on this issue with the precise wording of the clause. A literal interpretation should be disregarded where the result is contrary to established legal precept (for example, an interpretation of the clause as establishing two competing applicable laws for interpreting the contract). However, it is unlikely that the holding in Shamil Bank could be extended to a more general proposition that contractual references to “Glorious Sharia” are merely assertions of a business’s quality or values. In Shamil Bank, the facts do not completely rule out the possibility that the parties may have intended for the Sharia to be given some regard when interpreting the contract.

Despite the Court of Appeal holding to the contrary, a Morabaha is generally recognized as more than a conventional sale agreement notwithstanding the controversy as to its effectiveness as a financing instrument compliant with Islamic law. The Court of Appeal’s restriction of the legitimate scope of the Morabaha may have influenced its view on the intent of the parties in referencing the “Glorious Sharia.” However, even if the Court of Appeal in Shamil Bank resolved the issues of intent in favor of the appellant-defendant, the uncertainty surrounding scope and content of Sharia law was dispositive on the issue of incorporation of the Sharia in interpreting the contract.

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62 Id. [52].
63 Id. [53]-[54].
64 See id. [6]-[9] (explaining that given that the agreement, and the performance thereof, had been subjected to the approval of the bank’s religious supervisory board and clear references to Islamic principles by the board in the certificate of compliance issued). Indeed, the Court noted that “[u]ntil their defenses were filed in this action, the [appellants] had never given any indication to the bank that they were dissatisfied on religious grounds with the arrangements agreed between the parties or that they sought to challenge them on the grounds that they did not comply with the principles of Sharia.” Id. [10].
65 See discussion supra Part IV.B.
V. CONTRACTUAL FOREIGN ILLEGALITY DEFENSES WHERE THE PLACE OF PERFORMANCE RECOGNIZES ISLAMIC PRINCIPLES

If a contract governed by English law requires performance in a country which recognizes Islamic principles, it is inevitable that issues of foreign illegality would arise. Foreign illegality defenses can be organized into two subcategories—substantive and procedural.

A. Applying a Foreign Illegality Defense on Substantive Grounds

In *Islamic Investment Company of the Gulf (Bahamas) Limited v. Symphony Gems N.V. & Ors.*, the High Court was asked to enforce payment of liquidated damages pursuant to a contract expressed to be a *Morabaha* agreement. The examination of a financial transaction structured in Islamic principles was a matter of first impression for English courts. Islamic Investment Company of the Gulf ("IIC") had entered into a *Morabaha* financing agreement with Symphony Gems ("Symphony") under which IIC was to provide a revolving purchase and sale facility to enable Symphony to buy precious diamonds. Under the agreement, Symphony, as a buyer, would identify and select the stones, which IIC would then purchase and immediately resell to Symphony at a pre-agreed profit margin. Under the contract, Symphony accepted responsibility for selecting gem suppliers and for payment to the suppliers regardless of any "defect, deficiency or any loss or any other breach" of a sale contract between a supplier and IIC. Symphony was also bound by the contract to pay IIC the full amount of the original price regardless of whether title or possession had actually passed to Symphony or IIC. Symphony’s rights were restricted by two independent provisions. Under the contract, IIC was not liable to Symphony for the condition or quantity of the goods and their compliance with whatever expectations or arrangements Symphony might have with the gem supplier. Although risk was to be assumed by IIC as long as it held title to the goods, it expressly disclaimed liability for any damage, loss or delay caused in transit. The contract was expressed to be governed by English law and subject to the exclusive jurisdiction of the English courts.

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67 Id. at 1–2, 13.
68 Id. at 12–15.
69 Id. at 4–6.
70 Id. at 5–6.
A supplier, Precious (HK) Ltd., was subsequently selected by Symphony and IIC made full payment to Precious. Symphony, however, refused to pay IIC, asserting that the goods had not been delivered. The court rejected Symphony's defense, holding that upon the proper construction of the contract, delivery was not a pre-condition to payment. Symphony also argued that the contract was unenforceable because part of the transaction took place under the laws of Saudi Arabia, where the contract would have been prohibited. Although the contract was governed by English law, Symphony argued that the English court should not enforce the contract because of its illegality in Saudi Arabia.

Symphony's unenforceability argument did not rely directly on Sharia principles. Instead, the defendants sought to rely on the English court's general disinclination to enforce a contract which is unlawful under some foreign law, which in this case was Saudi Arabian law that codifies Sharia principles. This disinclination, though expressed as being based on international judicial comity, is not an inflexible rule. A good measure of judicial discretion is normally injected into the decision-making process. An English court will always look at the substance of the illegality in question and what English public policy dictates. The court in Lemenda Trading Co. Ltd. v. African Middle East Petroleum Co. noted:

The English courts should not enforce an English law contract which fails to be performed abroad where: (i) it relates to an adventure which is contrary to a head of English public policy which is founded on general principles of morality, and (ii) the same public policy applies to the country of performance so that the agreement would not be enforceable under the law of that country.

In such a situation international comity combines with English domestic public policy to militate against enforcement. Of the two factors, English domestic public policy emerges as the dominant force that

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72 Id. at 23.
73 Id. at 24–25; see also Regazzoni v. K.C. Sethia (1944) Ltd., [1958] A.C. 301 (H.L.) (explaining that English courts will not enforce contracts when the enforcement thereof involves acts performed in a foreign country and which are illegal in that country).
74 Mahonia Ltd. v. JP Morgan Chase Bank, [2003] EWHC (Comm) 1927, [16]–[17] (internal citations omitted).
77 Id.
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determines if enforcement will occur.

The Commercial Court rejected Symphony’s argument, stating that part of the transaction claimed by Symphony to have some connection with Saudi Arabia was so minor that the principle of foreign illegality could not justifiably be invoked. The court found that the agreement did not call for any performance by the parties in Saudi Arabia. The fact that IIC was based in Saudi Arabia and that the contract offers and acceptances were faxed to and from IIC in Saudi Arabia was insufficient to assert the principle of foreign illegality. Moreover, Symphony was a Belgian company and the only non-payment obligations to be performed under the agreement were to be performed by Symphony in Belgium.

The foreign law argument in Islamic Investment Company of the Gulf failed because there was no real nexus between the performance of the contract in question and the country where the contract would have been illegal. However, in other factual circumstances, the principle of foreign illegality may provide an alternative defense to breach of contract, when a choice of law or incorporation defense is likely to fail because of poor contract drafting. The success of a foreign illegality defense depends on whether the foreign illegality coincides with English public policy. In Mahonia Ltd. v. JP Morgan Chase Bank, in dismissing a preliminary application strike out defense, the Commercial Court held that as a matter of law, a letter of credit issued to support an underlying contract that was unlawful under U.S. law could not be enforced. The letter of credit in question was required to set up a cosmetic scheme to pass off certain accounts as healthy, in violation of securities law in the United States. Thus, despite the principle of autonomy, the court held that a letter of credit would be unenforceable if tainted by foreign illegality. Although the underlying contract was legal in England, an English court would not, in principle, support the commission of an offense abroad in the place of

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79 Id.
81 Mahonia, [2003] EWHC (Comm) 1927, [24], [28]–[29]. The alleged purpose for entering into the three swap transactions was to enable one party (Enron) to obtain a loan without disclosing the loan to the SEC. The omission was allegedly contrary to United States GAAP Financial Accounting Standard Board statement 133 and therefore, it would have been against U.S. securities laws for Enron to fail to disclose the loan in filings with the SEC. The conduct with intent to defraud could lead to criminal and civil liability under the United States Securities Exchange Act. Id. [5].
82 Id. [39].
There are significant barriers to succeed on a defense of foreign illegality. Based on the holding in *Mahonia*, an English court might be expected to be hesitant to apply the principle of foreign illegality where the illegality is a mere technical offense or one which finds little correspondence or recognition in English public policy as inappropriate conduct. This result is even more likely when the contract at issue is explicitly expressed to be governed by English law. Furthermore, English courts are not prepared to undertake a legal evaluation as to whether a foreign law has actually been breached. However, much depends on the weight of evidence. The High Court held that evidence presented before the court at trial was insufficient to determine whether an offense under the United States Securities Exchange Act of 1934 (and violation of the relevant United States version of Generally Accepted Accounting Principles ("GAAP")) had been committed by the parties. The court would not therefore deny enforcement of the letter of credit which underpinned that transaction. Although it might be argued that the court’s unwillingness was influenced to a large extent by the principle that the letter of credit is autonomous, it is likely that the court erred on the side of non-enforcement because the underlying conduct is prohibited in the United States and not under English law.

An English court would be far more likely to find foreign illegality in cases concerning contracts expressed to be governed by the foreign law, or in cases concerning contracts presumed to be governed by a foreign law according to the Contracts (Applicable Law) Act 1990 ("the Act"). Articles 8 and 10 of the Rome Convention, as given effect to by the Act, provide that a contract which is unenforceable under its applicable law would also normally not be enforceable in England. This outcome is

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83 Id. [16].
85 Mahonia Ltd. v. JP Morgan Chase Bank, [2004] EWHC (Comm) 1938, [422]–[434] (Eng.).
87 Article 8(1) states: "The existence and validity of a contract, or of any term of a contract, shall be determined by the law which would govern it under this Convention if the contract or term were valid." Rome Convention, *supra* note 4, art. 8(1). Article 10(1) states:

The law applicable to a contract . . . shall govern in particular:
tempered by an element of judicial discretion. English courts have consistently ruled that a finding of foreign illegality will not occur if the foreign law is one which English law rejects on grounds of public policy or substantial justice.  

B. Applying a Foreign Illegality Defense on Performance Grounds

Under Article 10(2) of the Convention, a court applying foreign law is required to consider “the law of the country in which performance takes place” when evaluating “the manner of performance and the steps to be taken in the event of defective performance.” Article 10(2) deals with the situation where the law of the country where performance takes place is different from the applicable law of the contract. How would an English court apply this provision? 

(a) interpretation; 
(b) performance; 
(c) within the limits of the powers conferred on the court by its procedural law, the consequences of breach, including the assessment of damages in so far as it is governed by rules of law; 
(d) the various ways of extinguishing obligations, and prescription and limitation of actions; 
(e) the consequences of nullity of the contract.

See, e.g., Heriz v. Riera, (1840) 59 Eng. Rep. 896 (Ch.); MacKender v. Feldia A.G. (1967) 2 Q.B. 590; In re Lord Cable, (1977) 1 W.L.R. (Ch.) (where the foreign law places on one or both the parties an unfair discrimination). See also Royal Boskalis Westminster N.V. v. Mountain, [1999] Q.B. 674; Kahler v. Midland Bank LD., [1950] A.C. 24 (H.L.) (where there is a vitiating factor, not recognized by the foreign law, but deemed wholly damaging to consent). The discretion of the court, however, would be narrowly applied. The approach is encapsulated by Judge Cardozo:

We are not so provincial as to say that every solution of a problem is wrong because we deal with it otherwise at home.... The courts are not free to refuse to enforce a foreign right at the pleasure of the judges, to suit the individual notion of expediency or fairness. They do not close their doors, unless help would violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common weal.

Loucks v. Standard Oil Co. of N.Y., 120 N.E. 198, 201–02 (N.Y. 1918).

See, e.g., Heriz v. Riera, (1840) 59 Eng. Rep. 896 (Ch.); MacKender v. Feldia A.G. (1967) 2 Q.B. 590; In re Lord Cable, (1977) 1 W.L.R. (Ch.) (where the foreign law places on one or both the parties an unfair discrimination). See also Royal Boskalis Westminster N.V. v. Mountain, [1999] Q.B. 674; Kahler v. Midland Bank LD., [1950] A.C. 24 (H.L.) (where there is a vitiating factor, not recognized by the foreign law, but deemed wholly damaging to consent). The discretion of the court, however, would be narrowly applied. The approach is encapsulated by Judge Cardozo:

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Loucks v. Standard Oil Co. of N.Y., 120 N.E. 198, 201–02 (N.Y. 1918).

Article 10(2) of the Rome Convention does not explicitly mention foreign law. However, if the applicable law is English (and not foreign), an English court would be bound to apply English law (as internal law) and not the private international law of England (of which the Rome Convention belongs). Additionally, Article 10(2) is read in conjunction with Article 10(1) which refers to “the law applicable to a contract by virtue of Articles 3 to 6 and 12,” and those provisions by and large refer to the selection or presumption of a foreign law. Rome Convention, supra note 4, arts. 3, 6, 10, 12. Rome Convention, supra note 4, arts. 3, 6, 10, 12.

Rome Convention, supra note 4, art. 10(2) (emphasis added).
court apply Article 10(2) to a contract governed by a foreign law (not of a country which has incorporated Islamic law) which requires payment to be made in a country where the payment of interest is prohibited or is limited?91

First, there is the issue of what is meant by "method and manner of performance." At common law, a clear distinction was made between obligations which were of the substance of the contract and obligations which were merely matters relating to the method or manner of performance. For example, in *Mount Albert Borough Council v. Australasian Temperance & General Mutual Life Assurance Society, Limited*,92 the New Zealand borough council had issued debentures charged at borough rates to an insurance company in Victoria, Australia. The interest rate on the debentures was five and two-thirds percent and payable in Victoria. In 1931, during the Great Depression, the Victoria legislature passed a statute reducing all mortgage rates to 5 percent. The court held that the statute did not apply to the debentures because although Victoria was the place of performance, New Zealand law was the proper law to apply when determining the interest rate of the debentures.93

Based on the reasoning in *Mount Albert*, it follows that the prohibition of or limitation on the payment of *riba*, and the rule barring penalties or fees for late performance,94 are not matters relating to the "method or manner of performance" but are matters of performance itself. The Giuliano-Lagarde Report offers some examples that illustrate the scope of Convention Article 10(2), such as rules governing public holidays, how

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91 In the United Arab Emirates, for example, Part 2 of the Commercial Code (Commercial Obligations and Contracts) states in Article 76 that "[a] creditor shall have the right to demand interest on a commercial loan in accordance with the rate stipulated in the contract . . . not [to] exceed 12 per cent." *THE LAW OF COMMERCIAL PROCEDURE OF THE UNITED ARAB EMIRATES: ISSUING LAW: FEDERAL LAW NO. 18 OF 1993, 46 (Dawoud Sudqi El Alami trans., 1993).* That said, the Dubai Court of Cassation, in Judgment No. 261/96, held that a creditor was entitled to collect 15 per cent interest on a debt the payment of which had been considerably delayed. *RICHARD PRICE & ESSAM AL TIMIMI, UNITED ARAB EMIRATES COURT OF CASSATION JUDGMENTS: 1989–1997 51–52 (1998).* Such recognition of commercial realities which clearly influenced the application of Islamic proscriptions is seen in a number of Islamic legal systems. Indeed, many such countries (e.g., Pakistan, U.A.E., Morocco, Qatar, Kuwait, Egypt) have made a clear distinction between civil and commercial matters, and have permitted to some extent foreign commercial and financial transactions to be exempt from the proscription against *riba* and *gharar*. See H. S. Shaaban, Comment, *Commercial Transactions in the Middle East, 31 LAW & POL’Y INT’L BUS. 157 (1999).* Be that as it may, that is not a certainty and the demarcation between foreign and domestic performance of the contract is not always entirely clear.


93 *Id.* at 231.

94 See, e.g., *THE QUR’AN* 2:280 (M.A.S. Abdel Haleem trans., 2004) ("If the debtor is in difficulty, then delay things until matters become easier for him.").
goods are to be examined, and the steps to be taken to reject the delivery of goods.⁹⁵ These examples illustrate that the less important details of performance are more likely to fall within the scope of Article 10(2).⁹⁶ A comparison with examples offered in support of Article 10(1) illustrates what is not classified as a “method or manner of performance”:

The diligence with which the obligation must be performed; conditions relating to the place and time of performance; the extent to which the obligation can be performed by a person other than the party liable; the conditions as to performance of the obligation both in general and in relation to categories of obligation (joint and several obligations, alternative obligations, divisible and indivisible obligations, pecuniary obligations); where performance consists of the payment of a sum of money, the conditions relating to the discharge of the debtor who has made the payment, the appropriation of the payment, the receipt, etc.⁹⁷

The examples given in the Giuliano-Lagarde Report for Article 10(1) explain the categories of what constitute “method or manner of performance” are extremely narrow.

Despite the absence of European Court of Justice and Member State case law defining the scope of Article 10(2), it does not appear that there is a significant difference between the common law and the Convention on the distinction between the substance of a contract and the method and manner of contract performance.

When performance of a contract takes place in a country governed by Islamic law, those laws will influence the analysis of contractual issues concerning the manner of performance or the steps to be taken in the event of defective performance. For example, application of Islamic law may affect the extent to which pre-payments or rebates are permitted⁹⁸ or what constitutes possession.⁹⁹ The degree of influence of Islamic law in these circumstances differs, depending on whether the Convention or common law principles are applied. Under Article 10(2) of the Convention, the court only needs to have regard for the law of the place of performance,¹⁰⁰ whereas at common law an English court was required to apply the law of the place of performance.¹⁰¹ There is little guidance as to how discretion

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⁹⁶ NORTH & FAWCETT, supra note 23, at 597.
⁹⁸ See USMANI, supra note 54, at 60–62; WAHBAH AL-ZUHAYLI, FINANCIAL TRANSACTIONS IN ISLAMIC JURISPRUDENCE 328 (Mahmoud el-Gamal trans., 2003).
⁹⁹ See USMANI, supra note 54, at 38.
¹⁰⁰ Rome Convention, supra note 4, art. 10(2).
should be exercised under Convention Article 10(2). The only assistance provided in the Giuliano-Lagarde Report is a brief exhortation that the court should do justice between the parties.102

An example of the common law doctrine of foreign illegality is found in Ralli Brothers v. Compania Naviera Sota y Aznar.103 In Ralli Brothers, the court held a contract unenforceable where performance of that contract was forbidden by the law at the place of performance. A carriage contract expressed to be governed by English law provided for the payment of freight on delivery of the cargo at Barcelona. The rate was set at £50 per ton. After the date of the contract, but before the vessel’s arrival, the Spanish government imposed a ceiling limit on the payment of freight. It decreed that it would be illegal to pay more than the equivalent of £10 per ton.104 The court dismissed the shipowner’s claim for the difference of freight, holding that the illegality under Spanish law should be recognized.105 However, as the contract in Ralli Brothers was expressed to be governed by English law, the “conflict” was between English law and the law of the place of performance. In such a case, as English law is the applicable law, the court is required to apply the internal law and not the private international law of England. It is not in fact a private international law issue. Instead, the issue in Ralli Brothers was one founded in the common law doctrine of frustration of contracts. Article 10(2), on the other hand, deals with the conflict between the applicable law of the contract and the law of the place of performance, a matter of private international law. The holding from Ralli Brothers is thus not directly applicable to a case evaluated under Article 10(2).106 It remains to be seen whether the courts will adopt the Ralli Brothers approach when applying Article 10(2).

There are two likely approaches that an English commercial court might contemplate when faced with such a situation, where the place of performance is in a foreign country governed by Islamic law. The first approach is to determine whether the law of the place of performance actually renders the manner of performance unlawful, and then rule accordingly. The second approach avoids making such a decision by construing the agreement in a manner to sidestep the issue,107 or by abusing
the discretion allowed under Article 10(2) and stating that in the eyes of English and the applicable law there was nothing unlawful about the manner of performance. The latter approach raises the issue of how judicial discretion should be exercised under Article 10(2). There are two possible methods of applying judicial discretion in tension with one another. The first method is to consider the parties’ presumed intention, that is to say, force of the contract. The second method is to apply the international comity principle; in other words, consider the wider interstate relationship and territorial interest of the state where performance is to take place. The Giuliano-Lagarde Report’s reference to “do[ing] justice between the parties” places the emphasis on the first method.\textsuperscript{108}

Therefore, the first duty of the court should be to give effect to the agreement as understood by the applicable foreign law. The court should then consider whether the manner of performance is contrary to the law of the place of performance, by evaluating whether illegality and the likely intervention of the country where performance takes place render performance an impossibility. It should be noted that English courts evaluating commercial cases may be inclined to save the contract at issue rather than to strike it down if the circumstances permit.\textsuperscript{109}

C. Judicial Treatment of Failed Foreign Law Arguments

In \textit{Islamic Investment Company of the Gulf}, the court emphasized that although the contract was governed by English law and interpreted under English law, the contract did not comply with Islamic principles because the required \textit{shurut} (conditions for the essential validity of the contract) were not present.\textsuperscript{110} While the court’s analysis on the compliance of the

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\textsuperscript{108} Giuliano-Lagarde Report, supra note 16, at 33.

\textsuperscript{109} See, e.g., Boyd & Co. Ltd. v. Louca, [1973] 1 Lloyd’s Rep. 209 (Com. Ct.) (Eng.) (holding that a contract calling for “F.O.B. stowed good Danish port” was not too uncertain to be enforced).

\textsuperscript{110} Islamic Inv. Co. of the Gulf (Bahamas) Ltd. v. Symphony Gems NV, 2001 Folio 1226, slip. op. at 12 (EWHC (Comm) Feb. 13, 2002), available at 2002 WL 346969 (no pagination available); also available at http://www.lawtel.com (original court transcript with page numbers) (“[I]t seems to me that it is not of any relevance to the issues which I have to decide what are the essential features of a Morabaha contract. The fact is that, as Dr. Samaan states and as I have no reason to think is in any way inaccurate, this contract does not have the essential characteristics of a Morabaha contract. Furthermore, it is a contract governed by English law.”). See also Umar F. Moghul & Arshad A. Ahmed, \textit{Contractual Forms in Islamic Finance Law and Islamic Inv. Co. of the Gulf (Bahamas) Ltd. v. Symphony Gems N.V. & Ors.: A First Impression of Islamic Finance}, 27 FORDHAM INT’L L.J. 150, 188–89 (2003–2004) (explaining that the goods were sent directly to Symphony Gems, bypassing Islamic Investment and the fact that Symphony Gems had no right to reject the goods if they proved to be defective). It should, however, be noted that Symphony Gems could have waived its Islamic rights and chosen to bear those responsibilities itself, but given the
contract with Islamic principles was unnecessary in reaching its verdict, the
analysis nonetheless lent a degree of moral support to the decision. The
court’s inclusion of this analysis demonstrates awareness of the sensibilities
of Islamic financiers and their traders and might refute charges of cultural
imperialism and failure to recognize the growing use of Islamic financial
structures.

VI. EXCLUSION OF LIABILITY CLAUSES AND THE MORABAHA
AGREEMENT

Morabaha agreements interpreted under English law risk running
afoul of laws prohibiting unfair contract terms. In many conventional trade
finance arrangements, the financing institution will insist on being insulated
from the sale transaction, because it does not want to assume the risk and
inconvenience of performance of the sale contract. For example, a letter of
credit arrangement achieves the removal of the risk and inconvenience by
entitling a bank merely to participate on the basis of the documents
relating to the sale. The principle of autonomy ensures that the bank
unequal bargaining positions of the parties and the absence of clear consent to the waiver,
the required shurut could not be said to be present.

111 Moghul & Ahmed, supra note 110, at 187.
112 See John H. Donboli & Farnaz Kashefi, Doing Business in the Middle East: A Primer
113 See Edward Owen Eng’g Ltd. v. Barclays Bank Int’l Ltd., [1978] 1 All E.R. 976, 983
(C.A.) (Eng.); see also R.D. Harbottle v. Nat’l Westminster Bank, [1977] 2 All E.R. 862,
870 (Q.B.D.) (Eng.); see also ICC Uniform Customs and Practice for Documentary Credits,
1993, Publication No. 500 (ICC 1993) [hereinafter UCP 500]. Under the UCP 500, banks,
for example, are absolved from responsibility for the effectiveness of the documents (Article
15), for any delays, errors, or failures in the transmission of messages or documents (Article
16), for the usual Acts of God (Article 17) and for errors or failures on the part of advising or
confirming banks they have selected in performing their instructions (Article 18(b)).
Furthermore, the applicant must indemnify the banks against all obligations and
responsibilities imposed by foreign laws and usages (Article 18(d)). The UCP 500 will soon
be superseded by another revision, the UCP 600. See The International Chamber of
Commerce, Banking commission approves revised rules on documentary credits, Oct. 25,
UCP 600 revisions).

114 See UCP 500, supra note 113, art. 4 (stating that the letter of credit is concerned not
with goods, services or other contractual performances, but with documents alone).
115 See id. art. 3:

(a) Credits, by their nature, are separate transactions from the sales or other
contract(s) on which they may be based and banks are in no way concerned with or
bound by such contract(s), even if any reference whatsoever to such contract(s) is
included in the Credit. Consequently, the undertaking of a bank to pay, accept and
pay Draft(s) or negotiate and/or to fulfill any other obligation under the Credit, is
not subject to claims or defenses by the Applicant resulting from his relationship
needs only to pay or refuse to pay on the basis of the documents. The bank is not involved with other details of the transaction such as the conformity of the goods.\textsuperscript{116} It is entitled to reimbursement from the buyer as long as it is able to demonstrate that the documents tendered by the seller are in conformity.\textsuperscript{117} It is not privy to the sale and would not be subject to the claims and defenses arising therefrom.

In comparison to conventional trade finance arrangements, a party to a \textit{Morabaha} arrangement is not as well insulated, because all participants are parties to the contract of sale and are therefore liable under the substantive terms of the sale contract. A financier seeking to avoid this type of liability might stipulate in the \textit{Morabaha} agreement that it is not liable under the contract of sale to the beneficiary of the financing (namely, the ultimate buyer) and that it would be merely liable to the supplier for payment of the price. Without this type of limitation, \textit{Morabaha} agreements might not be commercially feasible. This limitation of liability would be delineated in the contract between the financer and beneficiary. For example, the financing institution in \textit{Symphony Gems} was made contractually exempt from liability for any “defect, deficiency or any loss” in the goods.\textsuperscript{118} In other words, the contract eliminated the financing institution’s liability for the condition or quantity of the goods or the description of the goods or any other terms which the buyer (Symphony) might have agreed to with the gem suppliers. Such an exclusion could run afoul of the provisions of the \textit{Sale of Goods Act 1979}\textsuperscript{119} dealing with the implied terms of title to sell,\textsuperscript{120} quiet

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with the Issuing Bank of the Beneficiary. (b) A Beneficiary can in no case avail himself of the contractual relationship existing between the banks or between the Applicant and the Issuing Bank.
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\textit{See, e.g.,} Hamzeh Malas & Sons v. British Imex Indus. Ltd., [1958] 2 Q.B. 127 (C.A.) (Eng.); \textit{see also} Equitable Trust Co. of N.Y. v. Dawson Partners Ltd., [1927] 2 Lloyd’s List L.R. 49 (H.L.) (U.K.); \textit{see also} Gian Singh & Co. Ltd. v. Banque de L’Indochine, [1974] 1 W.L.R. 1234 (P.C.) (U.K.).\textsuperscript{116} On the principle of autonomy, \textit{see generally} Edward Owen Eng’g Ltd. v. Barclays Bank Int’l Ltd., [1978] 1 All E.R. 976 (C.A.) (Eng.).\textsuperscript{117} \textit{See, e.g.,} Kwei Tek Chao and Others (Trading as Zung Fu Co.) v. British Traders and Shippers Ltd., [1954] 1 All E.R. 779 (Q.B.D.) (Eng.) (noting that the shipping documents (such as the bill of lading) revealed that the goods were shipped late); \textit{see also} New Chinese Antimony Co. v. Ocean Steamship Co., [1917] 1 K.B. 664 (C.A.) (Eng.) (noting that the quantity did not correspond with the contract quantity); \textit{see also} C. Groom, Ltd. v. Barber, [1915] 1 K.B. 316 (K.B.D.) (Eng.) (noting that the insurance cover where required was inadequate); \textit{see also} J.H. Rayner & Co. v. Hambros Bank Ltd., [1943] K.B. 37 (Eng.) (noting that the description of the goods did not correspond with the contract description).\textsuperscript{118} \textit{Islamic Inv. Co. of the Gulf (Bahamas) Ltd. v. Symphony Gems NV}, 2001 Folio 1226, slip. op. at 5 (EWHC (Comm) Feb. 13, 2002), \textit{available at} 2002 WL 346969 (no pagination available); \textit{also available at} http://www.lawtel.com (original court transcript with page numbers).\textsuperscript{119} \textit{Sale of Goods Act 1979}, c. 54 (U.K.).\textsuperscript{120}
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possession,\textsuperscript{121} description,\textsuperscript{122} and satisfactory quality.\textsuperscript{123} Parties can never contractually agree to waive or restrict the conditions of title to sell and quiet possession. The Unfair Contract Terms Act 1977\textsuperscript{124} states that description and quality liability under non-consumer contracts of sale "can be excluded or restricted by reference to a contract term, but only in so far as the term satisfies the requirement of reasonableness."\textsuperscript{125}

\begin{footnotesize}
\textsuperscript{120} Id. \S\ 12(1) (providing that "there is an implied condition on the part of the seller that in the case of sale, he has a right to sell the goods, and in the case of an agreement to sell, he will have a right to sell the goods at a time when property is to pass"); see Niblett, Ltd. v. Confectioners’ Materials Co., [1921] 3 K.B. 387 (C.A.) (Eng.) (holding that where the goods sold had infringed a third party’s trademark, the seller could not be said to have a right to sell those goods).

\textsuperscript{121} Sale of Goods Act 1979, c. 54, \S\ 12(2) (U.K.) (stating that "there is also an implied warranty that—(a) the goods are free, and will remain free until the time when the property is to pass, from any charge or encumbrance not disclosed or known to the buyer when the contract is made, and (b) the buyer will enjoy quiet possession of the goods except so far as it may be disturbed by the owner or other person entitled to the benefit of any charge or encumbrance so disclosed or known"); see Empresa Exportadora de Azucar v. Industria Azucarera Nacional S.A., [1983] 2 Lloyd’s Rep. 171 (C.A.) (Eng.) (holding that as the seller had connived at securing a governmental decision to withdraw and seize the goods already sold, that was sufficient to constitute a breach of \S\ 12(2)(b)).

\textsuperscript{122} Sale of Goods Act 1979, c. 54, \S\ 13(1) (U.K.) (stating that where there is a contract for the sale of goods by description, there is an implied condition that the goods will correspond with the description, and that if the sale is by sample as well as by description it is not sufficient that the bulk of the goods correspond with the sample if the goods do not also correspond with the description). See Ashmore & Son v. C.S. Cox & Co., [1899] 1 Q.B. 436 (Eng.) (holding that in international sales, especially documentary sales, a stipulation as to time for shipment will form part of the description of the goods, and failure to ship within the shipment period would constitute a breach of condition).

\textsuperscript{123} See generally Sale of Goods Act 1979, c. 54, \S\ 14 (U.K.).

\textsuperscript{124} Unfair Contract Terms Act 1977, c. 50 (U.K.).

\textsuperscript{125} Id. \S\ 6(3). \textit{See also} id. \S\ 6(3), sched. 2. Schedule 2 of the Unfair Contract Terms Act 1977 lays down some guidelines to ascertain what meets the requirement of reasonableness:

The matters to which regard is to be had in particular... are any of the following which appear to be relevant—

(a) the strength of the bargaining positions of the parties relative to each other, taking into account (among other things) alternative means by which the customer’s requirements could have been met;

(b) whether the customer received an inducement to agree to the term or in accepting it had an opportunity of entering into a similar contract with other persons, but without having to accept a similar term;

(c) whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealings between the parties);

(d) where the term excludes or restricts any relevant liability if some condition is not complied with, whether it was reasonable at the time of

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Are the exclusions in Morabaha agreements, such as those in Symphony Gems, reasonable under the Unfair Contract Terms Act 1977? One indicator of reasonableness is that the customer has been given an inducement to accept the so-called unfair contract term. Because the bank would not have financed the customer without the exclusion or limitation of liability clauses, the financing itself might be thought of as inducement to accept these limiting contract terms. Another indicator of reasonableness is awareness or knowledge of the unfair contract term in question. Parties to Morabaha agreements should be fully aware of the need for such clauses in order to make the agreements commercially viable. Additionally, the parties specifically opted for a Morabaha agreement instead of a traditional commercial letter of credit arrangement in order to comply with Islamic law. It would be hard to argue that parties choosing a specific form of contract are unaware of the terms of that contract. Therefore, both indicators of the reasonableness exclusion or limitation of liability clauses are present.

On the other hand, some Islamic jurists have commented that a true Morabaha agreement cannot contractually limit the financer’s duties as a seller. Even if the Morabaha has alternate uses as a financing instrument, it is still, in essence, a sale contract, and it is not acceptable to modify a Morabaha agreement to mimic a conventional financial instrument. In other words, a Morabaha agreement is sui generis and should thus be recognized and applied as such. An English court adopting this view might find it harder to allow the terms excluding or limiting liability under the Sale of Goods Act 1979, because the indicators supporting a finding of reasonableness (inducement and knowledge/awareness) are far less persuasive if the resulting instrument is not viewed by Islamic jurists as a true Morabaha agreement.

The analysis under the Unfair Contract Terms Act 1977 may not apply in all cases. International supply contracts are excluded from its scope. An “international supply contract” is defined as “(a) either (i) a contract of sale of goods or (ii) one under or in pursuance of which the possession or ownership of goods passes; and (b) it is made by parties whose places of business (or, if they have none, habitual residences) are in the territories of the contract to expect that compliance with that condition would be practicable; (e) whether the goods were manufactured, processed or adapted to the special order of the customer.

Id. § 6(3), sched. 2(b).

Id. § 6(3), sched. 2(c).

See generally Moghul & Ahmed, supra note 110, at 172–74.

Additionally, an international supply contract must also meet one of the following conditions:

(a) the goods are, at the time of the conclusion of the contract, in the course of carriage, or will be carried, from the territory of one state to the territory of another; or

(b) the acts constituting the offer and acceptance have been done in the territories of different states; or

(c) the contract provides for the goods to be delivered in the territory of a state other than that within whose territory those acts were done.

Exclusion and limitation of liability clauses in international supply contracts would therefore not be subject to the reasonableness test laid down by the Unfair Contract Terms Act 1977. Without this reasonableness test, exclusion and limitation of liability clauses will be valid so long as they have been properly incorporated into the contract.

It is often the case that the financing bank and the ultimate buyer are established in the same country. For example, an importer based in the United Kingdom seeking a Morabaha agreement for financing is likely to work with a financing bank established in the United Kingdom as well. As the contracting parties are within the same state, the exclusion in Section 26 of the Unfair Contract Terms Act 1977 would not apply, and the contract is subject to a reasonableness test. The same analysis applies to Morabaha agreements, even if the goods are actually "bought" from a foreign third party supplier, because the relevant contracting parties for the Section 26 exclusion are the importer and financing bank, not the importer and the supplier.

Moreover, Section 26 of the Unfair Contract Terms Act 1977 refers to an international sale of goods contract. Is a Morabaha agreement a sale of goods contract? In Shamil Bank, because the court insisted on some

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130 Id. § 26(3).
131 Id. § 26(4).
132 Where the Unfair Contract Terms Act 1977 does not apply, the validity of the exclusion or limitation of liability clause will be determined by the common law. Under the common law, there is no test for reasonableness or unconscionability. The courts will approach the contractual clause purely as a matter of construction. See Photo Prod. Ltd. v. Securicor Transp. Ltd., [1980] A.C. 827 (H.L.) (appeal taken from Eng.) (U.K.) (rejecting reliance on a fundamental breach doctrine to negate an "unfair" clause, and holding that it was fallacious to assume that such a clause would not exclude liability for a fundamental duty; whether or not an exclusion clause applied to a breach, whether fundamental or not, was a matter of construction of the clause in question).
134 Id.
genuine connection between the bank and the subject matter, it was clear
that the court interpreted the *Morabaha* agreement as a sales contract
instead of a finance instrument. A court will not assume that all
agreements expressed to be *Morabaha* agreements are sales contracts; it
makes this determination based on the facts of the individual case.

**VII. IMPORTING ISLAMIC CONCEPTS OF FAIRNESS INTO CONTRACT INTERPRETATION**

If the scope of a court's reasonableness inquiry expands from
individual contract terms to evaluation of the contract as a whole, a court
might consider broader Islamic concepts of fairness when evaluating the
fairness of the contract. If it is clear that the parties to a contract had
expectations of performance based on Islamic principles, and intended to
contract based on those principles, a court should incorporate analysis of
Islamic principles in its evaluation of the fairness of the contract. Ignoring
the relevance of those principles would prevent a court from gaining a
complete understanding of the full factual matrix of the contract at issue.

From a policy standpoint, incorporating Islamic principles in a fairness
evaluation would address criticism that western courts are making Islamic
jurisprudence irrelevant to issues of Islamic finance.

**VIII. EXTRA-JUDICIAL REVIEW OF ISLAMIC FINANCE CONTRACTS**

Many financing arrangements in the Middle East and elsewhere in the
Islamic world require monitoring by a religious supervisory board. The
parties must agree by contract to give force to the decisions and
recommendations made by the relevant board. This can be accomplished by
allowing appropriate sanctions. Alternatively, the parties may give the

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135 [2004] EWCA (Civ) 19, [13]–[17], [47] (Eng.).
136 An English court would not accept a label as determinative of the character of the contract. See, e.g., Comptoir D'Achat et de Vente du Boerenbond Belge S/A v. Luis de Ridder Limitada, [1949] A.C. 293, 293–94 (H.L.) (appeal taken from Eng.) (U.K.) (holding that despite the contract in question being labeled and referred to as an Ex Ship contract, it was in substance a CIF contract).
137 See, e.g., Phillips Products Ltd. v. Hyland, [1987] 2 All E.R. 620 (C.A.) (Eng.) (holding that in examining whether the test of reasonableness has been satisfied, the court has to determine all of the relevant circumstances and whether those circumstances were or should have been known to or contemplated by the parties at the time the contract was made).
139 Such religious supervisory boards might operate under the state's auspices or within the bank's own internal structure.
board power to order a new contract to replace an existing one and to make
relevant changes to the contract, even after the contract has been made.\textsuperscript{141}
In \textit{Shamil Bank}, the system of religious supervision was ineffective because
it applied to the general activities of the bank instead of the specific
agreements into which the bank entered.\textsuperscript{142}

While direct monitoring of agreements by a religious supervisory
board might be more effective, this option is not entirely free from practical
difficulties or doctrinal controversy. The involvement of a religious
supervisory board not only lengthens and complicates the negotiation and
contracting process, it also leads to commercial uncertainty because the
board may be given the ability to re-write the contract.\textsuperscript{143} Decisions of a
religious supervisory board might be questioned before the Islamic courts
or religious authorities of the countries in question, further reducing the
certainty of contracts between parties.\textsuperscript{144}
IX. CONCLUSION

Shamil Bank confirms that the Rome Convention does not allow non-country specific law to be the applicable law of the contract. Parties to a contract cannot choose Sharia law per se or English law as guided by Sharia principles. One possible solution, therefore, is that parties operating in the U.K. market who wish to deal on Islamic principles should adopt choice of law provisions that incorporate the law of a country that most closely gives effect to the Sharia principles with which they are concerned.145 However, English law and English private international law, as contained in Article 10(2) of the Rome Convention, encourages courts to consider the law of the jurisdiction where performance takes place.146 This means that a court may hesitate to apply a choice of law provision with a result that would contravene the applicable law in the place of performance. Therefore, the obstacle presented by Article 10(2) and the foreign illegality principle would have to be overcome in order for this to be an effective solution to the incorporation of Islamic principles in a contract.

Alternatively, parties can adopt a clause subjecting the contract to a set of expressed terms and conditions compliant with Islamic principles, such as a code of industry practice adopted by Islamic banks, or a specific set of rules established by an individual Islamic bank.147 Regardless of the fact that the terms might draw on Islamic law and practice, incorporation of the terms into the contract is permissible under English law because the relevant terms are clearly identifiable. However, the incorporation of Islamic principles as a matter of contract might be perceived by some as the relegation of Islamic law to nothing more than a set of contractual terms. This can cause problems for the Islamic financiers seeking to secure the business of more orthodox Islamic traders, and their stakeholders, who are unhappy to see Islamic law being treated as less than binding legal rules which should be accorded the same recognition as the law of a sovereign

http://www.thedailystar.net/2006/07/03/d6070301033.htm (reporting the disagreement between banks and the Bangladeshi Islamic Supervisory Council (set up by the Government) over matters of interpretation). Indeed, the Institute of Islamic Banking and Insurance, London, has seen fit to publish a selection of such Sharia rulings. See A COMPENDIUM OF LEGAL OPINIONS ON THE OPERATIONS OF ISLAMIC BANKS (Yusuf Talal DeLorenzo ed., 1997).

145 In Shamil Bank, Bahrain, while embracing and encouraging Islamic banking practice as a national policy, did not incorporate the principles of Islamic law, in particular the prohibition of riba, into its commercial law, and there is an absence of any legal prescription as to what does and does not constitute “Islamic” banking or finance. In other Middle Eastern countries, banking interest is tolerated (Saudi Arabia) and even sanctioned by banking laws (Bahrain, Qatar and Oman, for example). See, e.g., COMMERCIAL LAW IN THE ARAB MIDDLE EAST: THE GULF STATES 133 (W.M. Ballantyne ed., 1986).

146 See Rome Convention, supra note 4, art. 10(2).

147 Adding specific Islamic-compliant contract language usually occurs after consultation with the country’s religious authorities and/or the bank’s own Religious Supervisory Board.
foreign state.

The failure to incorporate Islamic principles into a Morabaha contract means that the contract is open to be treated solely by English law. Serious implications arise as a result. First, that means the contract is likely to be treated as a sale of goods contract subject to the Unfair Contract Terms Act 1977 and the Sale of Goods Act 1979. Second, although an argument can be made that the "restrictive" terms of the Morabaha might satisfy the reasonableness test of the Unfair Contract Terms Act 1977, it is by no means incontrovertible. Third, a Morabaha agreement, though involving the import of foreign goods, could very well be classified as a domestic contract under Section 26 of the Unfair Contract Terms Act 1977 because the importer and the financing bank are based in the same country. In such a case, the Morabaha contract could not evade the provisions of the Unfair Contract Terms Act 1977 in order to benefit from the common law's lax approach to exclusion and limitation of liability clauses contained in international supply contracts.

Globalization will require the international commercial environment to recognize and integrate both Islamic and conventional forms of commerce and finance. Courts in non-Islamic countries must therefore rise to the challenge of giving proper effect to Islamic financing or commercial arrangements. The challenge for international commercial lawyers is to find a way to incorporate Islamic principles in a manner in which the courts would be able, both legally and practically, give effect. No English court will enforce an ambiguous or unclear legal and commercial instrument, whether compliant with Islam or not. More debate is needed on whether and to what extent lawyers who, having recognized the distinctive expectations of Islamic traders, should westernize the contracts by using hermetically sealed choice of law or other clauses. Such an approach may pre-empt the problems following a dispute, but it adds little to facilitate the smooth performance of the contract. While this article has focused on crafting Islamic-compliant contracts that survive judicial scrutiny, the contract drafter must also focus on the clear articulation of the expectations.

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150 See Unfair Contract Terms Act 1977, c. 50 (U.K.).
153 Id.
of the parties so as to ensure success of the commercial transaction.\textsuperscript{156}

\footnotesize{\textsuperscript{156} See Berthold Goldman, \textit{The Applicable Law: General Principles of Law—the Lex Mercatoria}, in \textit{Contemporary Problems in International Arbitration} 125 (Julian D.M. Lew ed., 1987) ("[L]aw is not only made of and for disputes . . . ").}