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MALAYSIA: LAW OF CHOICE FOR ISLAMIC FINANCE AND CENTRE FOR DISPUTE RESOLUTION

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I have spoken or written on this topic a number of times since 29 July 2010 when I spoke on *"Interface Between Shari'ah and Civil Law In Islamic Finance: Current Problems and the Way Forward"* at the Malaysian Law Conference. I developed the theme in my 12th Emeritus Professor Ahmad Ibrahim Memorial Lecture on 7th December 2011 titled *"Malaysia as An Islamic Finance Hub: Malaysian Law as the Law of Reference and Malaysian Courts as the Forum for Settlement of Disputes"*.

I will just summarise the points that I have made all these years. Those who want to read more may visit my website: www.tunabdulhamid.my

In GIFF 2012 I argued on *"The Need for Shari'ah Compliant Law of Choice for Islamic Finance Transactions."* I think that there is such a need is beyond dispute. The question is, it there any country in the world that can say *"We have a complete Shari'ah compliant law for Islamic finance, including documentation of the contracts and settlement of disputes in the courts of law."* I don't think there is.

However, having that alone is not enough. There are other factors. Those are the factors that make parties currently choose the law of and the courts in England and New York as the law of choice and the forum for settlement of disputes, in spite of the fact that they do not offer Shariah-compliant laws and that their courts would not apply the Shari'ah. Those factors are actually partly facts and partly perception.

So, the challenge is which country could produce a system which satisfies the two sets of requirements? A country which succeeds in doing so, in my view, will be the winner. I would like to see that that country is a Muslim majority country. Otherwise, *"We are an ummah of lost opportunity,"* to quote Sheikh Nizam Yaakubi.

Speaking about Malaysia, of course, at this point of time, we are not in a position to say that all our laws as are applicable to Islamic finance are Shariah-compliant, but I think we are very close to it.

Regarding the application of Shari'ah, unlike the English courts, no court in Malaysia has said that Shari'ah willl not be applied if the contract says it will be applied. On the other hand, in a few cases, the High Court had held that the transaction was not Shariah-compliant. The defence that a contract is void because it is contrary to Shai'ah is a common defence put up by the defendants and they are considered on merits.

The passage in my judgment in ***Bank Kerjsama Malaysia Bhb v. Emcee Corporation Sdn Bhd*** (2003) 1 CLJ 625 (C.A.) has often been quoted but, unfortunately, without paying attention to the facts. The passage reads:

"As was mentioned at the beginning of this judgment the facility is an Islamic banking facility. But that does not mean that the law applicable ***in this application*** *is different from the law that is applicable if the facility were given under conventional banking. The charge is a charge under the National Land Code. The remedy available and sought is a remedy provided by the National Land Code. The procedure is provided by the Code and the Rules of the High Court 1980. The court adjudicating it is the High Court. So, it is the same law that is applicable, the same order that would be, if made, and the same principles that should be applied in deciding the application."*

The point I would like to stress here is that, in that case, the applicable laws were the same as the laws applicable in a conventional banking case. That is because the issue was whether an order for sale (foreclosure order, in England) should be granted or not. That was all. No one raised any Shari'ah issue, no one argued that the laws mentioned were not Shariah-compliant. The fact that the same laws are applied in conventional cases does not make them Shariah-non-compliant that they cannot be applied in Islamic banking cases.

Unfortunately, everybody quotes that passage as if I was saying that in all Islamic finance cases, only civil law applies. Lawyers and judges are trained to analyse and reason, not to read and repeat. Imams read and repeat.

We realised quite early that our civil court judges were unqualified to make rulings on Shari'ah issues. So, in a paper dated 9 February 2002, I made the suggestion that Shari'ah issues that arise in the courts should be referred to the Shari'ah Advisory Council (SAC) of the Central Bank. My proposal was accepted and it became law. (Later a similar provision was made for cases under the Securities Commission (SC) to be referred to the SAC of the SC). That provides for consistency of the rulings by a group of experts in Shari'ah, Islamic finance and others. Quite a lot has been written on the SAC. You may find mine on my website.

So far 6 references have been made by the court and one by the arbitrators. I am told that there are requests to refer to the SAC from other government agencies and even foreign governments and foreign financial institutions which the SAC is not legally empowered to accept and therefore had to be turned down. The SAC had on 19th June 2012, issued its *Manual Rujukan Mahkamah dan Penimbang Tara Kepada Majlis Penasihah Syari'ah Bank Negara Malaysia (Manual by which the Court and Arbitrators May Refer Shari'ah Matters to the Shari'ah Advisory Council of Bank Negara Malaysia).* It provides the procedure for making references. I believe that it is the first of its kind in the world.

Of course, challenges were made on constitutional ground. Until today, the highest court that had decided on it is the Court of Appeal. The Court of Appeal affirmed the constitutionality of the law. One case that went up to the Federal Court was settled out of court. So, the Court of Appeal's judgment stands.

I have the advantage of seeing references of Shari'ah issues by the court to the SAC as an idea; of making the proposal and was accepted; of seeing the idea becoming law; of seeing the challenges mounted against it; of seeing the amendment to incorporate my earlier suggestion which was not agreed earlier after a High Court judgment; of seeing it enacted in the new law (Islamic Financial Services Act 2013

Act 759) and a similar provision in the Capital Markets and Services Act 2007 (Act 671). As a member of the SAC, I was involved in the making of the Manual by both the SAC of BNM and SC. When references were made by the Court and the Arbitrators to the SAC of Bank Negara, again as a member of the SAC, I was involved in the deliberation and the drafting of the answers to be given. I am convinced that we have done the right thing.

Next, through the establishment of the Law Harmonisation Committee (LHC), we try to identify laws applicable in Islamic finance transactions which are not Shari'ah-compliant and amend them to make them Shariah-compliant. We also try to identify laws which are not conducive to the development of Islamic finance and try to improve them. I'll just mention one example that has been done i.e. the introduction of the after judgment late payment charge in the Rules of Court, comparable to "interest after judgment" applicable in conventional cases. The reason was because customers were using the loop-hole to delay and avoid settling their judgment debts arising from Islamic banking cases. The reason is simple: the longer they delay the more they "gained."

I first publicly made the proposal for a rule of court to be made for this purpose in my paper *titled "Interlink/Interface Between Civil Law System and Shari'ah Rules and Principles and Effective Dispute Resolution Mechanism"* at the Islamic Financial Services Industry Legal Forum on 28 September 2009.

That was the first thing I took up when I was appointed Chairman of the LHC a year later. We applied the principles of *ta'wid* and *gharamah*. The *ta'wid* portion goes to the judgment creditor and the *gharamah* portion goes to charity. I am happy to see Order 40 rule 12A in the Rules of Court 2012. It came into force on 1 August 2012 and is now in operation. On 31st January 2013, the Central Bank issued a Guidelines on Late Payment Charges for Islamic Financial Institutions as a guide to the industry on the application of the new O.40 r.12A ROC 2012. I understand that it is working smoothly.

We already have a sufficiently large number of Shari'ah Scholars who are fluent both in English, Arabic and Malay and who are also knowledgeable on the working of Islamic banking, Islamic finance and takaful. I think they are among the best in the world.

Regarding judges and arbitrators, actually their job is made easier because they may refer Shari'ah issues to the SAC. What they have to know is the nature of a product and its mechanism in order to be able understand the non-Shariah issues and decide on them. In this respect the Judiciary is very cooperative. Seminars continue to be held to educate the Judges.

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Unfortunately we still do not have a sufficient number of litigation lawyers who are well versed in the subject. I would like to see more Muslim Lawyers in this area bearing in mind that it is faith–based. Unfortunately, they are not forthcoming. It seems, again it is a case of *"an ummah of lost opportunity".*

With regards to other factors, I think we already have them. Let us take a quick look at them:

1. Malaysia, in the eyes of the world, is an Islamic country. Internationally, it is seen as model Islamic country. It is only natural for Malaysia to want to be the hub for Islamic finance.

2. Malaysia is already the leader in Islamic finance.

3. No other Government in this world has done more than the Malaysian Government in developing and for the development of Islamic finance. Our Universities offer a wide range of Islamic finance subjects. INCEIF is one of its kind in the world. It is supported by ISRA.

4. We already have the common law and the common law system in place and working comparatively well.

5. Malaysian lawyers and Judges speak English, our laws and judgments of our superior courts are in English.

6. Our courts and arbitrators are comparatively efficient, competent and independent. Their knowledge of the subject is at par, if not better than their counterparts elsewhere. With the introduction of the Certificate in Islamic Banking and Finance for Arbitration program by INCEIF in co-operation with Chartered Institute of Arbitrators (CIArb), we hope to better prepare our arbitrators for the challenges ahead.

7. We have the infrastructure. Our court rooms are among the best in the world, our transportation and communication are good, our streets and hotels are free from suicide bombing (so far), our cost of living is comparatively cheap and we have summer throughout the year, which is not very severe. All these factors are conducive to foreign lawyers coming to do litigation here.

With all these factors in our favour, I think we are moving in the right direction towards achieving that objective. You may think that it is a tall order. But, at least we dare to think and work for it. Remember what people thought about Japanese-made cars when they were first brought to Malaya to compete with Austin, Morris, Hillman and Consul, the big names from England in early 1960s. Where are those big names now? Think of the Japanese-made motor cycles when they were imported to compete with Norton, Triumph, Royal Enfield, BSA and Ariel, the big names from England then. Where are those big names now?

Thank you.

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