DISPUTE RESOLUTION IN ISLAMIC BANKING AND FINANCE: CURRENT TRENDS AND FUTURE PERSPECTIVES

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Abstract

The current legal framework for dispute resolution in the Islamic banking and finance industry in developing countries may not adequately serve the purpose for which the financial institutions were set up. Meanwhile, the Islamic legal framework for dispute resolution has established rules for financial disputes as recognized under the classical law. This paper examines the current practice of dispute resolution in Islamic banking and finance with case analyses of selected Muslim countries. From our findings, disputes emanating from this industry are heard by the conventional courts and tribunals which, in most cases, do not have the requisite expertise. It is argued that since Islamic banking and finance disputes are sui generis, the panel of judges must be composed of experts in the field. The paper concludes that a legal framework should be established for dispute resolution in countries where Islamic banking and finance is being implemented. For a proper Islamization of the banking and finance sector, disputes arising from this sector should not be subjected to the convoluted conventional rules. The paper proposes a legal framework for dispute resolution in the Muslim world based on hybrid processes of Alternative Dispute Resolution (ADR) recognized in Islamic law.

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1. INTRODUCTION

The re-emergence of Islamic banking and finance in the global scene has come with different types of new financial products.¹ This practice has crystallized with the proliferation of Islamic financial institutions all over the Muslim world and beyond. With these developments, an inevitable phenomenon in financial transaction in form of disputes, claims or complaints is a recurring decimal in the industry. The clear tilt in the economic balance presently in favour of the Muslims may be jeopardized if proper legal framework is not established for the resolution of the disputes emanating from the Islamic banking and finance industry. As an alternative to the court system where most judges sitting in the bench are not conversant with the technical terms and products involved in Islamic financial services, an independent body can be established to serve as the leading body for resolution of disputes at the regional levels. The modus operandi of the Alternative Dispute Resolution (“ADR”) to be adopted by this body should be based on the principles of sulh, tahkīm, muhtasib and a hybrid of some of the processes recognized in Islamic law.

It is important to categorically state that without the establishment of a specialized body within the regions where Islamic banks and financial institutions are situated across the world, the full realization of total Islamization of banking and financial transactions will never be realized. The current practice where Islamic banking and finance disputes are heard and determined by the civil or common law courts with lopsided judgments will be counter-productive to the practice of Islamic banking and finance.

Against the above backdrop, this paper examines the current trends in the resolution of Islamic banking and finance disputes as well as the future perspectives. Following a chronological order, section two of this paper dilates on the re-emergence of Islamic banking and finance in the modern world with so many innovative financial products. Matters arising from litigating Islamic banking and financial disputes, claims and complaints are closely considered in section three. Furthermore, section four discusses the re-emergence of Alternative Dispute Resolution processes in the modern world and the

classical methods available within the ambit of Islamic law. Section five proposes an international legal framework for the resolution of Islamic banking and finance disputes, claims and complaints.

My charge here is not to cheerlead, but to critically assess the current state of things in the resolution of disputes within the Islamic banking and finance industry. We must develop an international legal framework for the resolution of the disputes since Islamic banking and finance disputes are of sui generis which requires special expertise. Though there are steps in some Muslim countries like Malaysia to set up some mediation-cum-ombudsman bodies to resolve banking and finance disputes, which includes the Islamic banks and financial institutions, it is argued that a great deal remains to be done through a proper legal framework for the resolution of the disputes.

2. RE-EMERGENCE OF ISLAMIC BANKING AND FINANCE

Though the entire Islamic history is replete with the practice of Islamic banking and finance in line with the legal texts in the Islamic corpus juris, it re-emerged on the global scene in the middle of the 20th century. This spurred the proliferation of Islamic banks and financial institutions within the Muslim world and beyond. The Islamic finance sector has now become the fastest growing industry in global finance in the wake of the economic meltdown. Without going very deep in recounting the detailed history of Islamic banking and finance, it suffices to chronicle certain developments that goaded its re-emergence in the modern world.

Islamic banking and finance has re-emerged in the global scene as a new reality to be reckoned with. The origin of it is found in the prime sources of the Sharī'ah as legislated by the Law-giver. The rightly-guided caliphs ardently practiced the basic principles of Islamic banking and finance as enshrined in the Qur’an and Sunnah on different scales. These legal precedents were closely followed and further developed by the succeeding generations in different forms. Therefore, the colonization of most

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2 The prohibition of interest or usurious transactions known as ribā is clearly explained in the Qur’an and Sunnah. Qur’an 2: 275 provides: “Those who eat Ribā (usury) will not stand (on the Day of Resurrection) except like the standing of a person beaten by Satan leading Him to insanity. That is because they say: "Trading is only like Ribā (usury)," whereas Allāh has permitted trading and forbidden Ribā (usury). So whosoever receives an admonition from his Lord and stops eating Ribā (usury) shall not be punished for the past; his case is for Allāh (to judge); but whoever returns [to Ribā (usury)], such are the dwellers of the Fire - they will abide therein." See generally, A.L.M. Abdul Gafoor, Interest-free commercial banking, (Kuala Lumpur: A.S. Noordeen, 2002). Also see Jamal al-Din ‘Atiyyah, al-Bunuk al-islamiyyah baina al-huriyyah wa tanzin al-taqlid wa al-ijithad al-nazariyyah wa tatbiq,(Qatar: Kitab al-Ummah, 1987).
Muslim territories and the fall of the Ottoman Caliphate in 1924 brought about the introduction of the conventional banking and finance system in most Muslim countries. Though the awareness was still there, the overwhelming effects of colonization affected the growth of Islamic banking and finance.

The resilience of Muslims in some Muslim countries brought about the re-emergence of the Islamic finance products in the 20th century. The first modern experiment of Islamic banking and finance can be traced to the Mit Ghamr Savings Bank in Egypt established in 1963 whose “purpose was to explore the possibilities of mobilizing local savings and credits as an essential requirement for socio-economic development in the area”. This experiment, which took the form of savings bank based on the principles of profit-sharing, lasted till 1967 and later, became a full blown bank in 1981 with branches across Egypt. Few years before the bank consolidated its services in 1981, other banks such as the Islamic Development (IDB) and Dubai Islamic Bank opened their doors to customers in 1975. Also, Malaysia followed suit with the enactment of the Islamic Banking Act 1983. This brought about the establishment of the first formal financial institution in Malaysia in 1983 known as the Bank Islam Malaysia Berhad (BIMB). However, before then, elements of the practice of Islamic finance have been recorded in Malaysia with the establishment of Pilgrims Management and Fund Board or the Tabung Haji in August 1969.

The growth of Islamic banking and finance products with some innovations is highly reassuring, and it signifies a skyrocketing boost in the sector. With so many Islamic banks and financial institutions and specialized windows springing up all over the world, a consistent growth rate of 10-15% per year has been recorded. It goes without saying that this important sector in global business needs a well streamlined framework for dispute resolution. It is unfortunate to observe that the banks cannot be fully “Islamic” if all incidental practices do not comply with Islamic law. Therefore, with the consolidation of Islamic banking and finance in the modern era, there is need for an

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3 For a detailed discussion on the evolution of Islamic finance in the global economy, see Ibrahim Warde, Islamic Finance in the Global Economy, (Edinburgh: Edinburgh University Press, 2000), pp. 73-89.
6 This is an Act specifically meant to provide for the licensing and regulation of Islamic banking business in Malaysia. It received Royal Assent on 9th March 1983, and was subsequently gazetted the following day.
Islamic legal framework for the resolution of disputes emanating from the industry through ADR processes recognized and practiced in Islamic legal history. It is in this sense we can then beat our chest with certainty that the whole banking and finance system has fully complied with the Islamic law of financial transactions. Dispute settlement is an inextricable part of Islamic law of transactions, and the Islamic banking and finance industry is a subset of the former.

3. CURRENT TRENDS IN LITIGATING ISLAMIC BANKING & FINANCE DISPUTES

The current legal framework for the resolution of disputes emanating from the Islamic banking and finance industry across the world cannot effectively serve the purpose for which the financial institutions were set up. The current trend of litigating Islamic banking and finance disputes does not augur well with the prospects of Islamization of the industry. Unfortunately, there are legal firms in the Muslim world that specialize in this area of legal practice. We make bold to observe that the idea of subjecting Islamic banking and finance disputes to court litigation, where many of those presiding do not have the requisite knowledge, is antithetical to Islamic law regulating dispute resolution. More often than not, the cases are usually between two Islamic financial institutions owned by Muslim majority shareholders. In this case, the simple rule of dispute resolution is to employ the legal processes sanctioned by the law rather than embracing the conventional litigious practice. While examining the constraints faced by the Islamic financial services in relation to dispute resolution, Engku Rabiah Adawiah observed thus:

In the case of disputes arising between an Islamic financial institution and its clients, they will have to refer the matter to the civil or common law courts that have jurisdiction to hear the litigation. This may result in decisions that may not comply with the Shariah rules. This problem is further exacerbated by the non-existence of any substantive law on Islamic financial services and banking practices in such countries. In short, although the transactions entered by the parties may be Shariah compliant in the first place, but upon enforcement of the contracts, the court may make orders and decisions that may sideline the Islamic legal principles.\(^8\)

This clog in the wheel of dispute resolution in Islamic banking and finance has cast some doubts in the full implementation of Shari‘ah-compliant products.

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After the enactment of the Islamic Banking Act 1983 and the consequent establishment of full-fledged Islamic Banks and Islamic windows in Malaysia, cases started emanating from the industry, and all the cases were heard and decided by the civil courts based on their outlandish rules that are strange to Islamic banking and financial transactions. Engku Rabiah Adawiah did a very good critique on a number of decided cases where she unravelled the inherent defects in the court decisions which is as a result of lack of expertise in the dynamics involved in the Islamic banking and financial services. We do not intend to repeat the critique but it is important to emphasize that a separate legal framework is essential for the proper Islamization of the banking and finance industry; or else, we shall continue to grope in the darkness of conventional rules while only succeeding in christening the financial services as “Islamic”.

In the first case on Islamic banking and finance ever heard and determined by the English court, Islamic Investment Company of the Gulf (Bahamas) Ltd v. Symphony Gems NV & Ors, a case of murabahah contract, the parties have agreed on the choice of law and jurisdiction as being the English law. After examining the nature and terms of the contract and listening to expert opinion, the court held that the English law principles of

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10 The Islamic banking and financial services cases that have been heard and determined by the civil courts in Malaysia include: Bank Islam Malaysia Bhd v Adnan bin Omar [1994] 3 AMR 44; Dato’ Hj Nik Mahmud bin Daud v Bank Islam Malaysia Bhd [1996] 4 MLJ 295 (High Court); and [1998] 3 MLJ 393 (Appellate Court); and Affin Bank Bhd v Zulkifli bin Abdullah [2006] 3 MLJ 67. It is submitted that in some of the decisions in these cases, the court did not make any reference to expert opinion, and the issues involve technical Islamic banking and finance products. In fact, in most cases, the judgment delivered by the court shows the shallowness of the knowledge of the judge, counsels and the parties on certain Islamic financial services which constitutes the subject matter of a dispute.


12 This is a unique mode of financing where the commodities are sold on a cost-plus basis. This is a form of credit sale “in which parties bargain on the margin of profit over the known cost price. The seller has to reveal the cost-incurred by him for acquisition of the goods and provide all cost-related information to the buyer.” See Muhammad Ayub, Understanding Islamic Finance, (England: John Wiley & Sons Ltd., 2007), p. 213.
contract must apply to the purported *murabahah* contract despite the fact that the expert opinion revealed that the agreement in issue did not have the essential characteristics of a *murabahah* contract. This is premised on clause 25 of the agreement which provides that “*[t]his Agreement and each Purchase Agreement shall be governed by, and shall be construed in accordance with, English law....*”\(^{13}\) With this clause, the parties have agreed that the transaction as well as any purchase agreement made pursuant thereto shall be governed and construed in accordance with the English law. In addition, clause 26 of the underlying agreement provides for an irrevocable submission to the jurisdiction of the English court. It is important to observe that in fairness to the English judges, party autonomy is of paramount importance in the choice of law and jurisdiction. Therefore, the court construed the agreement as an English law contract which validated the seemingly invalid *murabahah* contract.

The above illustration gives an insight into the problems faced in the proper implementation of Islamic banking and financial services in situations where parties subject themselves to the jurisdiction of courts who have little or no knowledge about Islamic law. This has been the trend in Islamic banking and finance cases before the English courts as further complicated in *Beximco Pharmaceuticals Ltd. & Ors v. Shamil Bank of Bahrain EC*\(^{14}\) where the English courts decided not to be concerned with or be bound by the principles of the Sharī‘ah in deciding the respective cases. This unfortunate situation is further highlighted thus:

This anomaly is further exacerbated by the choice of the parties to be adjudicated by a non-Islamic court in a non-Islamic jurisdiction, who may not give due recognition and enforcement to the Islamic legal principles in arriving at the judgment. As a result, a transaction that is non-compliant with the Shariah may still be validated and enforced by the court of law. This will translate into the bank being able to recover the amount claimed, ie, its selling price inclusive of profits, despite the transaction being non-compliant with the Shariah. If this is the result of the judgment order, the noble aim of having Islamic banking and financial services that comply with the Shariah will be defeated.\(^{15}\)

It is hoped that this incongruity in the implementation of Islamic financial services will be corrected and properly streamlined to reflect the best practices in the industry by adopting a legal framework for dispute resolution based on Islamic law.

\(^{13}\) Ibid.
\(^{14}\) [2004] EWCA Civ 19 (Court of Appeal, Civil Division); [2004] All ER (D) 280 (Jan).
\(^{15}\) Engku Rabiah Adawiah bt Engku Ali, n. 8 at p. xxix.
4. THE EMERGENCE OF ALTERNATIVE DISPUTE RESOLUTION

4.1 The Paradigm Shift in Dispute Resolution

After the long practice of litigation in most developed countries, people realized the inherent evils and the effects of the litigious virus on the relationship of people in the society. Gradually, there was a paradigm shift from court adjudication to alternative methods in the 20th century. Though the idea has been there for quite some time, major reforms began towards the setting up of court-connected dispute resolution mechanisms through amendments of court rules and enabling legislations. “The advent of ADR represents a global dissatisfaction with the litigation process because of its attendant delays, protractedness, costliness and acrimonious nature.”

This new trend in developed and developing countries across the world has favoured ADR processes and particularly, the use of hybrid procedures in dispute resolution. Though there are numerous ADR processes used in the conventional practice of dispute resolution, the scope of this paper is limited to the ADR processes within the Islamic legal paradigm.

4.2 An Overview of the Relevant ADR Processes in Islamic Law

Amicable dispute resolution in Islamic law is as old as Islam itself when one critically considers the Islamic legal history particularly in relation to commercial transactions as well as political feuds. The Islamic corpus juris is replete with legal texts prescribing processes such as sulh, tahkīm, muhtasib, and hybrid processes for the settlement of disputes in an amicable manner. These ADR processes are considered as “basic tenets” of civil justice in Islamic law. This extra-legal settlement of disputes has strong support in the two prime sources of Islamic law to encourage people to always bury the hatchet as much as possible. From the viewpoint of Islamic law, the following represent the recognized processes of dispute resolution:

(i) Sulh (good faith negotiation, mediation/conciliation, compromise of action);

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19 Syed Khalid Rashid, n. 17 at p. 96.
 Though most of the processes may directly or indirectly apply to Islamic banking and finance disputes, it is expedient for us to focus on the relevant processes for the sake of an evaluative assessment.

With the complexities involved in Islamic banking and finance disputes, it is expedient to devise hybrid ADR processes “which carries all the goodness of amicable resolution with the end-result possibility of a fast-track arbitral award when every other effort fails to produce a result”. However, before we discuss the hybrid processes most appropriate for Islamic banking and finance disputes, it is apposite to briefly appraise some relevant ADR processes recognized in Islamic law to serve as a background discussion before the proposition of some hybrid processes.

4.2.1 Sulh

The basic method of dispute resolution particularly in commercial and financial transactions is good faith negotiation generally referred to as sulh. In Arabic philology, the word “sulh” in the context of interpersonal relationship is from the generic word “salaha” which means “to make peace, become reconciled, make up, reach a compromise or settlement”. However, in the classical Islamic thought and tradition, sulh means the amicable settlement of disputes through good faith negotiation, conciliation/mediation, peacemaking, and even extends to compromise of action. This is an institutionalized method of dispute resolution recognized and prescribed by the primary sources of the Sharī’ah. In most cases, sulh takes the nature of a binding contract on the parties

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20 Ibid.
involved, as it is usually described as an agreement between two or more parties to end a dispute by addressing its cause(s) with a view to ending it finally.\footnote{See Ahmad Abu Al-Wafa, *Kitab Al-I'laam Bi-qawa'id Al-Qanun Al-Dawli Wa Al-Alaaqat Al-Dawlayah Fi Shari'at Al-Islam*, p. 39, cited in Said Bouheraoua, “Foundation of Mediation in Islamic Law and Its Contemporary Application”, paper presented at the 4th Asia-Pacific Mediation Forum Conference which was hosted by Harum Hashim Law Centre, Ahmad Ibrahim Kulliyyah of Laws, International Islamic University Malaysia, between 16–18 June 2008.}

The primary sources of the Shari'ah strongly promote amicable settlement in all circumstances based on equitable, fair and just manner with the ultimate end of justice through a win-win result.\footnote{Qur'an 49: 9-10 provides: And if two parties or groups among the believers fall into a quarrel, then make peace (sulh) between them [...] with justice, for Allah loves those who are fair (and just). * The believers are but a single brotherhood, so make (peace and) reconciliation (sulh) between two (contending) brothers, and fear Allah, that you may receive mercy. Also see, Qur’an 4:114. See generally, F. Ali, “Conflict –Its Psychological Causes, Effect and Resolution Through the Qur’an”, paper presented at the Conference on Conflict Resolution in the Arab World, Cyprus, August 1993.} Apart from the numerous legal texts of the Qur’an prescribing sulh, the Sunnah is also replete with practical approaches towards the proper establishment of the institution of sulh.\footnote{Mohammed Abu-Nimer, “Conflict Resolution in an Islamic Context –Some Conceptual Questions ”, *Peace & Change*, January 1996, p. 35.} For instance, Sahl bin Sa’ad has narrated that there was a intra-tribe dispute amongst the tribe of Amr bin ‘Auf, and the Prophet immediately set out for the sole purpose of making sulh among them.\footnote{The full text of the Hadith is given in *Sahih al-Bukhari*. See Muhammad Muhsin Khan, trans. *The Translation of the Meanings of Sahih al-Bukhari*, (Beirut: Dar al-Arabia, n.d.), p. 531.} There are procedural as well as substantive rules regulating the process of sulh which are fundamentally premised on the precedents in the Islamic legal history particularly the period of the Prophet Muhammad (S.A.W.) and the four rightly-guided caliphs.\footnote{The details of the substantive rules as well as the procedural rules are outside the scope of this research since our aim here is to propose a legal framework for the resolution of Islamic banking and financial disputes. It is when this framework has been established we can then proceed to consider the intricacies involved in the procedural rules. However, in the penultimate section of this paper, we shall examine some hybrid processes of dispute resolution within the context of Islamic law in relation to the Islamic banking and finance disputes.}

Though sulh is generally conducted in an informal manner, the law allows institutionalized sulh to facilitate the process of settlement and ensure the enforceability of any agreement reached between the contending parties. Even within the institutionalized framework that is being proposed in this research, there is always unencumbered emphasis on informalism in the procedural rules. In relation to Islamic banking and finance disputes, sulh is a veritable gold mine that should be explored as a first step towards the resolution of disputes. This will be very relevant in bank-and-customer relationship disputes. In addition, disputes between two financial institutions can be easily resolved through well-coordinated good faith negotiation. An important caveat that
must be added in the case of financial disputes is that the underlying contract from where the dispute emanated must be legal in the eyes of the Sharī’ah. This is based on the famous letter written by Caliph Umar b. al-Khattab directed to Abu Musa al-‘Ash’arī on the latter’s appointment as a judge. The Caliph highlighted a number of rules relating to administration of justice. One of the numerous rules relates to sulh, and it provides:

All types of compromise and conciliation (sulh) among Muslims are permissible, except those that make what is lawful prohibited or makes what is prohibited lawful.²⁹

This is based on an authentic Hadīth of the Prophet which Caliph ‘Umar quoted to remind Abu Mūsā al-‘Ash’arī of his duty. This provision is of a general application which serves as a binding precedent on modern practice of sulh.

4.2.2 Tahkīm

Though the concept of tahkīm as a process of dispute resolution has been widely practiced in the pre-Islamic Arabia, the advent of Islam gave it firm support and further streamlined the procedure to ensure fair dealing and justice. To this end, there are direct indications to the use of tahkīm as a process of dispute resolution in the primary sources of the Sharī’ah. In its simplest form, tahkīm means arbitration. It has been described as “the spontaneous, and more or less improvised, move by two or more parties in dispute to submit their case to a third party called a hakam or muhakkam (arbitrator).”³⁰ Such a reference of dispute to a third party neutral for settlement based on the provisions of Islamic law occupies an important position in dispute resolution within the context of Islamic law.³¹ There are basically three legal texts in the Qur’ān that gives approval for arbitration:

If you fear a breach between them twain (the man and his wife), appoint (two) arbitrators, one from his family and the other from her’s; if they both wish for peace, Allah will cause their reconciliation. Indeed, Allah is Ever All-Knower, Well-Acquainted with all things.³²

²⁹ This is the text of a Hadīth related by al-Tirmidhi, Abu Dawud, Ahmad and Ibn Majah.
³² Qur’ān, al-Nisāʾ : 35.
But no, by your Lord, they can have no Faith, until they make you judge in all disputes between them, and find in themselves no resistance against your decisions, and accept (them) with full submission.  

Verily! Allah commands that you should render back the trusts to those to whom they are due; and that when you judge between men, you judge with justice. Verily, how excellent is the teaching which He (Allah) gives you! Truly, Allah is Ever All-Hearer, All-Seer.

From the first legal text, one may assume that arbitration is only prescribed in family disputes. This notion is not correct, as application of arbitration extends to commercial, financial and civil disputes. Regarding the binding nature of *tahkîm*, there are two major views: the first view believes it is not binding as it can be regarded as conciliation or amiable composition. This view is based on the first legal text of the Qur’an quoted above which gives the notion of non-binding proceedings. Conversely, the second view, which is premised on the provisions of the second and third verses quoted above, holds that an arbitral award is binding on the parties. Though there are numerous opinions among the respective schools of thought in Islam, once an arbitral award is filed in court for the purpose of recognition and enforcement, and the judge (*qâdî*) is satisfied that there is no error in the award on the point of law, it will become binding on the parties. The controversy is settled thus:

Hanafis and Shafi’is hold that arbitration is very close to compromise. The arbitral award is binding only if the parties agree. Thus arbitration is like conciliation. Followers of this view hold that if an arbitral award is regarded as binding, this would challenge the authority of the State, the judge and ultimately of the *imam* (sultan). Both Malikis and Hanbalis hold the view that the decision of an arbitrator is binding unless it contains a flagrant injustice. However, once the arbitral award is filed in the Court of a *qâdî*, it becomes binding, if *qâdî* finds no fault in it.

An important issue raised here is related to the nature of arbitral proceedings. The duty of an arbitrator is likened to that of an “amiable compositeur” because in *tahkîm* the arbitrator is legally required to use his discretion, sense of fairness, justice, equity and

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33 Qur’an, al-**Nisā’**: 65.
34 Qur’an, al-**Nisā’**: 58.
35 On the scope of *tahkîm* in Islamic jurisprudence, see Umar A. Oseni, n. 31 at p.p. 77 – 79.
37 Syed Khalid Rashid, n. 17 at p. 104.
indeed, public policy in resolving the dispute. The only proviso to this blank check is that any award given must not infringe on any principle of the Sharī’ah.\(^{38}\)

### 4.2.3 Med-Arb

As the names implies, Med-Arb is an acronym of two previously discussed processes of dispute resolution —Mediation and Arbitration. Within the context of Islamic law, Med-Arb is the hybrid of both the *sulh* and *tahkīm* processes in order to arrive at an amicable resolution of the dispute. This hybrid process is well-known within the conventional practice of ADR. However, the Med-Arb process has been recognized and prescribed by the Qur’an and it was practiced in the Islamic legal history. The practice has been one of the main dispute resolution techniques in Islamic law since over 1,400 years ago.\(^{39}\) The basis of Med-Arb is given in the following legal text as contained in the Qur’an:

> If you fear a breach between them twain (the man and his wife), appoint (two) arbitrators, one from his family and the other from her’s; if they both wish for peace, Allah will cause their reconciliation...\(^{40}\)

The latter part of the text gives an indication to the effect that if during the proceedings any of the parties or both wish for reconciliation rather than an arbitral award through a compromise, then Allah will guide them to such reconciliation. Therefore, it is always emphasized that the arbitrator must begin with suggestions of possible moves towards reconciliation before embarking on the arbitral proceedings.\(^{41}\) The mechanism of the Med-Arb process within the context of Islamic law has been explained in a previous research thus:

> The Med-Arb process is a mechanism for dispute resolution enmeshed within the general framework of *Sulh* (amicable settlement) in Islamic jurisprudence. *Sulh* is a broad term which literally means amicable settlement. Its juristic meaning is all-embracing as it includes good faith negotiation, mediation/conciliation, and compromise of action.\(^{42}\) In most cases during the *Tahkīm* proceedings, both *sulh* and *tahkīm* are combined to facilitate the process of dispute resolution. This is encouraged in most cases because employing the Med-Arb process is considered an obligation for the arbitrators in Islamic jurisprudence.\(^{43}\)

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\(^{38}\) Ibid. Also see Qur’an, *al-Nisā’: 58* which provides: "Verily! Allah commands that you should render back the trusts to those to whom they are due; and that when you judge between men, you judge with justice. Verily, how excellent is the teaching which He (Allah) gives you! Truly, Allah is Ever All-Hearer, All-Seer."\(^{38}\)

\(^{39}\) Umar A. Oseni, n. 31 at p. 99.

\(^{40}\) Qur’an, *al-Nisā’: 35.*

\(^{41}\) Syed Khalid Rashid, n. 17 at p. 110

\(^{42}\) *Id,* at pp. 96 – 97.

\(^{43}\) Umar A. Oseni, n. 31 at p. 99.

4.2.4 Muhtasib

In ensuring administrative justice, the institution of ombudsman has become a veritable tool for both the private and public sector to resolve disputes amicably and ensure ongoing business relationships. Within the context of Islamic law, the institution of ombudsman is known as muhtasib though with certain variations in the duties of the latter compared to the former. Though the institution of ombudsman emerged in its present form in Sweden as established in 1809,\footnote{The popular legal historical background for the institution of ombudsman has its source in the Justitieombudsman created in Sweden in 1809. He was given the important task of prosecuting culpable administrators and judges. Etymologically, “Ombudsman” is a Swedish word which means a representative or agent of the people or group of people. The modern Swedish ombudsman ensures that public office holders respect the law and properly fulfill their entrusted obligations. Mary Seneviratne, Ombudsmen – Public Services and Administrative Justice, (United Kingdom: Reed Elsevier (UK) Ltd., 2002), p. 1; and Mary Seneviratne, Ombudsmen in the Public Sector, (Buckingham: Open University Press, 1994), p. 2.} there has been earlier practice of ombudsman with wider jurisdiction in the Islamic legal and political history in form of muhtasib. One of the main general functions of a muhtasib is to regulate commercial activity within the state by protecting the interest of the consumers and the entrepreneurs alike, and guard public interest with much emphasis on administrative justice.\footnote{See generally, Athar Murtuza, “Muhtasib’s Role: Safeguarding the Public Interest during the Islamic Middle Ages” (2004). American Accounting Association 2004 Mid-Atlantic Region Meeting Paper. Available at SSRN: http://ssrn.com/abstract=488882.}

Specific duties of a muhtasib include taking account (hisbah) of issues that relate to “weight and measures, quality of commodities on sale in markets, honesty in trade and commerce, observance of modesty in public places, and such other things both temporal
and spiritual.” The unique nature of the functions of a muhtasib can be seen in its two important elements of dispute avoidance and dispute resolution. The origin of muhtasib is found in the prime sources of the Sharī‘ah. There are numerous legal texts of the Qur’an that provide for the institution of muhtasib. It suffices to cite this:

Let there arise out of you a group of people inviting to all that is good (Islam), enjoining what is right and forbidding what is wrong. And it is they who are the successful.

The above legal text from the Qur’an lays down the general law regulating the establishment of the institution of muhtasib in a State. The Prophet Muhammad practically carried out these divine enactments by appointing ‘Umar bin al-Khattāb as the muhtasib of Madīnah, while Sa‘ād bin al-‘Ās bin Ummayyah was delegated as a muhtasib to Makkah. The whole institution of muhtasib is to carry out the sacred duty of enjoining good and forbidding evil for the general benefit of all. This is however carried out through the processes of dispute resolution and dispute avoidance in line with the Sharī‘ah. From the foregoing, it is clear that the general powers vested in the office of a muhtasib are wider in scope than the modern ombudsman because the former’s powers cover both spiritual and temporal affairs. A muhtasib has a great role to play in Islamic banking and finance disputes because of the informal nature of dispute resolution and avoidance and the friendly procedure adopted in the process.

4.2.5 Fatāwā of Muftīs

The need for expert determination of disputes through a process of evaluation cannot be overemphasized in the modern mechanisms of dispute resolution. Fatāwā of a Muslim jurists represents three evaluative assessment of a dispute which may involve evaluative mediation, mini-trial or expert determination. Hence, fatāwā can be described as “the issuance of nonbinding advisory opinions (fatāwā, or fatwās) to an individual questioner.

47 Syed Khalid Rashid, n. 17 at p. 111.
48 Ibid.
49 Qur’an, al-Imrān: 104. Also see Qur’an 4:110 and 114; Qur’an 9:71; and Qur’an 31:17.
52 Syed Khalid Rashid, n. 17 at p. 113.
53 Id., p. 115.
(mustafīṭ), whether in connection with litigation or not\(^{54}\). The nonbinding advisory opinion may even be sought by two contending parties or a group of people who have certain differing opinions on an issue. This process of dispute resolution is similar to Expert Determination used in the conventional practice of ADR.

Expert Determination is a process “where parties to a dispute entrust it to some expert for evaluation in view of the technical nature of the dispute”\(^ {55}\). This form of consensual ADR allows a third party neutral jointly appointed by the disputing parties to make an evaluative assessment of the rights and duties of the latter based on the basis of objective criteria. There is a difference between Expert Appraisal and Expert Determination on the basis of the binding nature of the evaluation. Generally, Expert Appraisal is not considered binding; and is only of persuasive value, while Expert Determination is usually binding on the parties when it is considered as a contract\(^ {56}\).

Within the context of Islamic law, the expert opinion of a jurist is useful in two instances: Dispute Avoidance and Dispute Resolution. In situations where a preemptive fatwa or nonbinding evaluation is taken form an expert and accepted by the parties based on their religious conviction, such evaluation is useful in dispute avoidance. Though such a fatwa is not binding on the parties like a judgment of a qāḍī, morality demands that since the parties appointed the expert, they should invariably accept his verdict.

Against the above backdrop, though the verdict or evaluation given by an expert is of persuasive nature and not considered binding, the significance of it is mostly felt in the area of dispute avoidance. This is an indispensable aspect of the phenomenon of dispute. The future of ADR in the modern world is a paradigm shift towards the evolution of dispute avoidance processes and not just mere emphasis on dispute resolution. Therefore, the fatāwā of an expert in form of non-binding evaluative opinion can be utilized to serve the golden purpose of dispute avoidance. This will be very useful within the Islamic banking and financial services where avenues may be provided for preemptory legal opinions on certain financial transactions that would have bred unwarranted disputes. However, the beauty of some of these processes of dispute resolution and avoidance can be better appreciated when practically used in a hybrid process.


5. TOWARDS AN INTERNATIONAL LEGAL FRAMEWORK FOR DISPUTE RESOLUTION

5.1 Setting the Scene for Institutionalized Legal Framework of Dispute Resolution

There has been a dramatic surge in the demand for an alternative to the current practice of subjecting Islamic banking and finance disputes to the regular courts. Even in countries like Indonesia where the Sharī‘ah Courts jurisdiction has been extended to include Islamic Banking and finance disputes, there is still a need for an alternative to court litigation or court-connected ADR processes premised on the principles of Islamic law.

The call for total Islamization of the banking and finance sector, at least, in Muslim-dominated countries will continue until such is achieved. It is not enough to propose this but there should be pragmatic steps towards the realization of the important objective. Hence, it is important to set the scene for an institutionalized legal framework for dispute resolution in the Islamic banking and finance province to standardize the best practices. In order to achieve this, it may be necessary to establish regional sulh centres across the world with branches in all the countries where there are functional Islamic banks and financial institutions. Such regional body may be established under the auspices of the Organization of Islamic Conference in cooperation with the Islamic Banks and Financial Institutions across the world.

There will be an urgent need of qualified human resources to man the offices across the world. Experts in Islamic banking and finance who have the requisite qualifications in Sharī‘ah will fit in as the pioneering staff. Thereafter, institutional training and standardization of best practices will be required. The requisite standards may be initially achieved, but there is need for the sustenance of such standard through the following:

(i) proper initial training;
(ii) initial post-training supervision;
(iii) formal accreditation;
(iv) on-going review and/or continuing education.\(^{57}\)

Though it is conceded that some people are naturally endowed with exquisite skills of dispute resolution, there is still the need for proper training to avoid using the dispute

\(^{57}\) This idea of standardization of best practices was inspired by the discussion in Andrew Zilinskas, “The Training of Mediators – Is It Necessary?”, *Australian Dispute Resolution Journal*, (1995), p. 63.
resolution process as “a minefield for untrained and unwary mediators.” This is because an effective mediator or dispute resolution expert must possess a combination of so many excellent human qualities as enumerated by Maggiolo:

(i) the patience of Job
(ii) the sincerity and bulldog characteristics of the English
(iii) the wit of the Irish
(iv) the guile of Machiavelli
(v) the hide of a rhinoceros
(vi) the wisdom of Solomon.

Therefore, the dispute resolution centre can be named “Regional Sulh Centre for Islamic Banking and Finance” which must have an autonomous international character. Meanwhile, we are not unmindful of the fact that the Kuala Lumpur Regional Centre for Arbitration in Malaysia came out with its Rules for Arbitration (Islamic Banking and Financial Services) in 2007. This move was initiated by Dato’ Rohana Yusof of Bank Negara in 2002. The rules incorporates the UNCITRAL Arbitration Rules of 1976 and makes it clear in Rule 48 that “[w]here these Rules are silent on any matter, the provisions under the UNCITRAL Arbitration Rules shall be applicable throughout provided the same is consistent with the Shariah”. These giant strides are highly commendable. However, there is room for improvement because despite the fact that the rules have been made, a number of parties still prefer to go to the courts or Financial Mediation Bureau (FMB). There is need for a standard legal framework, at the international level, for dispute resolution of Islamic banking and finance disputes.

5.3 The Hybrid ADR Processes in Islamic Banking and Finance Disputes

In order to search for viable hybrid processes for dispute resolution in Islamic banking and finance, it is important to keep certain basic considerations in mind. The interest of the parties is very crucial to an amicable resolution of a dispute. Islamic banking and finance disputes are of a special nature, so, there is need for neutral parties who have the requisite expertise in the field to preside over the settlement of the dispute. However, it is

58 Id, p. 59.
important to make the procedure cost-effective and consensus building to enhance and fast-track the process to ensure ongoing business relationship. In situations where the parties have not reached a consensus, it is apposite to hybridize the process by bringing in a binding third party decision such as arbitration, expert determination or even the ombudsman.\textsuperscript{62}

An attempt to resolve Islamic banking and finance disputes with an individual process of dispute resolution like \textit{tahkīm} or \textit{sulh} may be counter-productive considering the nature of financial disputes which sends shivers down the spines of many disputants. No individual, entrepreneur or financial institution will want to take any huge financial risk. Therefore, two hybrid processes are being proposed for the settlement of Islamic banking and finance disputes. The first is an amalgam of the triad consisting of mediation (\textit{sulh}), expert determination (\textit{fatāwā}) and ultimately, arbitration (\textit{tahkīm}). On the other hand, parties may opt for the Med-Muh hybrid procedure which is more appropriate for the settlement of disputes between a customer and his/her financial service provider. These two hybrid processes may be incorporated into the institutional rules of the proposed “Regional \textit{Sulh} Centre for Islamic Banking and Finance”.

\textbf{5.3.1 Med-Ex-Arb}

As a preliminary step, it is always better to begin dispute resolution proceedings with \textit{sulh} which is termed “mediation’ for the purpose of the hybrid process. There is emphasis in the Qur’an on the preference of \textit{sulh} as a first step towards the amicable resolution of any dispute. In order to ensure a well reasoned decision, it is proposed that such good faith negotiation-cum-mediation should be supported by a binding Expert Determination. Such experts should be known for their expertise in the field of Islamic banking and finance and all other related financial transactions. This is similar to the current practice, though through court litigation, where some legislations allow the court to state a case to a particular Sharī‘ah Advisory Council. For instance, Section 16B(8)(b) of the Central Bank of Malaysia Act 1958 (Revised 1994) provides that the court must make reference to the National Sharī‘ah Advisory Council on any proceedings before it which relates to Islamic banking and finance for its ruling. Any ruling therefore “made by the Sharī‘ah Advisory Council pursuant to a reference made under paragraph (8)(b) shall, for the purposes of the proceedings in respect of which the reference was made –if the reference was made by a

\textsuperscript{62} See Syed Khalid Rashid, n. 21 at p. 8.
court, be taken into consideration by the court in arriving at its decision.”  

However, in the model we are proposing, the hybrid process starts with *sulh* and if such is not successful within a reasonable time, the dispute should proceed for binding Expert determination. This will be carried out by such expert who is learned in Islamic banking and financial services and has the requisite training-cum-expertise of dispute resolution. The same panel can conduct the *sulh* phase of the process and thereafter proceeds to Expert Determination. After an objective evaluation of the case, the experts give their opinion which is considered binding because the whole process will be based on a contractual agreement *ab initio*. Such expert opinion may assist in nipping the conflict in the bud. However, if the any of the parties to the dispute refuses to be guided by the opinion of the expert by accepting the decision, there is always the need for an enforceable procedure in form of *tahkīm*. This will give the whole process a force of law and such decision/expert opinion will be summarily converted to an award and it becomes enforceable.

5.3.2 Med-Muh

Med-Muh is a mixture of mediation (*sulh*) and *muhtasib*. This amalgam is more relevant in the resolution of administrative-cum-financial disputes, claims or complaints which generally arise out of bank-customer relationship. As a preliminary step, such a hybrid process will begin by utilizing the *sulh* process before proceeding to the institution of ombudsman (*muhtasib*). Normally, the *muhtasib*, who should have the requisite expertise of dispute resolution within the context of Islamic law as well as working knowledge of the dynamics in Islamic banking and finance transactions, must begin the proceedings by adopting the *sulh* mechanism. This will be conducted between the person who lodged the complaint and the relevant financial services provider. If the dispute, complaint or claim is not resolved or any of the parties is not satisfied, then, the *muhtasib* will decide the matter based on his assessment and applying the relevant laws from the Islamic perspective. The decision of the *muhtasib* is binding on the parties and no appeal can be made against such a decision. The decision of the *muhtasib* should not be subject to any judicial review because his decision is of arbitrative value. The decision of ombudsman can be enforced by any competent court.

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64 See Ibid., Section 16B(8)(a)(b).
6. CONCLUSION

In this paper, I have advocated the need for a framework for the resolution of disputes emanating from the Islamic banking and finance industry across the world. Such move should be based on the classical means of dispute resolution recognized in Islamic law. The kind of framework proposed is a hybrid dispute resolution mechanism that will conveniently be utilized in resolving the disputes owing to the fact that disputes from the industry are somehow complex. With this in mind, the Islamic financial service industry will be saved from the claws of court litigation which is always accompanied by unnecessary negative stereotyping which may not be favourable in terms of marketing.

The enduring nature of the dispute resolution processes recognized and practiced in the Islamic legal history makes a case for their relevance in the modern era. We cannot continue to grope in the darkness of court litigation. It is time for the regional or international regulating bodies for the Islamic banks and financial institutions to grope for inspiration from the Islamic law practice of dispute resolution based on the hybrid processes explained above. Doing so will be a big leap in the direction of easy settlement of claims within the industry.
REFERENCES


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