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The Methodology of Product Development Needed for Islamic Banks Upholding Social Responsibility

Part 1

Paper presented at the International Conference on Business Ethics and Corporate Social Responsibility: Ideals and Realities, organized jointly by IGIAD –Society for Economic Entrepreneurship and Business Ethics (Iktisadi Girisim ve Is Ahlaki Dernegi), Istanbul and Durham Centre for Islamic Economics and Finance, Durham University, UK, 12th-14th April 2012, Istanbul University Main Campus, Istanbul, Turkey.

Abstract

Unarguably the current methodology of product development in Islamic finance has failed to reflect the social dimension embedded in Islamic economics. This is evidenced by the nature of the current financing products in Islamic banks being hardly distinguishable from that of conventional products, according to critics and observers. Therefore, a substantial change is required in this methodology in order to observe the social responsibility while structuring a financing product. This entails the departure from the notion that bases the legality of the product on its structure without considering its essence and implications. The new methodology however must not overlook the positive and sound aspects of the current methodology of product developing, since this methodology has undoubtedly yielded some good products and helped fulfill basic Shariah requirements in transactions. Therefore, a reform rather than a replacement of this methodology is required. For outlining the new reformed methodology, the article starts by stating the basic Shariah requirement in financial contracts, whose fulfillment ensures consistency with the social mission of Islamic Finance. It then examines the current methodology used for developing financing products in Islamic banks in order to identify its flaws. After identifying the flaws the paper investigates and discusses the justifications provided by the Islamic financial institutions for neglecting the Shariah elements whose absence has led to stripping Islamic finance of its socially constructive nature. In light of the discussion, the article works on laying down the basics of a new methodology which upholds the social responsibility and still takes into account the constraints facing the proper application of Islamic finance.

Manuscript Type: Analytical; Empirical.

Purpose: This paper aims to highlight the shortcoming of the current methodology used for structuring Islamic financing products in order to propose a sound one that involves a social good.

Design/methodology/approach: Critical; Constructive.

Research Finding/Result: A modified methodology for product development.

Research limitations/implications: Substituting the current methodology used in Islamic finance with the proposed one.

Practical Implications: Having genuine Islamic financing products with social good.

Originality/Value: Important for the credibility of Islamic banks and development of the Muslim societies.

Keywords: Shariah; Islamic Finance; Methodology of Product Development; Social Responsibility; Social Good, Contract Substance; Contract Structure.

I. Introduction

The issue of social responsibility of Islamic banking and finance has been in focus recently. This in general reflects two things: the type of expectations Muslims had from Islamic banking, and the failure of Islamic banks to perform their perceived social role. However, it is really unclear whether the social good is something embedded in the Islamic financial transactions so that whenever they are applied on banking scale a social good is to be expected, or that the social good is something Islamic banking should undertake and seek after since it is not embedded in the transactions per se! Should the latter be true, one, on the other hand, should not overlook the fact that Islamic banks are not charitable institutions, but rather profitable ones entrusted with investing depositors' money, and that the absence of independent charitable organizations, whose establishment is the responsibility of the Muslim treasury under the Muslim state, must not place the blame on Islamic banks. The query however remains valid if upholding a social responsibility comes at no additional financial cost or loss to Islamic bank and remains a matter or preference influenced by extra caution and subjective assessment of the potential returns.

To give a fair answer, however, to the query raised above, Islamic financial transactions in general if executed properly, genuinely and with full observance of their Shariah rules and conditions does carry within some embedded good. Nevertheless, contracts remain merely tools so they need to be directed to serve a particular purpose. If this purpose has to be the social good, then it must be set in advance and worked on, but Islamic banks would not be then doing something against Islamic banking nature, but rather they would only be administering malleable ingredients.

However, the question is: Are Islamic baking willing to undertake a social responsibility?

As a matter of fact, the Muslim public has legitimate demands and rights over Islamic banks. If these demands are met, the social good will come about automatically. These legitimate demands relate to the right application of Shariah rules since the very using of ISLAM as a slogan gives the right to all Muslims to demand from these commercial initiations full adherence to the Islamic Shariah. They also relate to selecting financing sectors that lead to some social good if doing so comes at no extra cost to Islamic banks. This right emanates from Islam being the religion of all Muslims and no one can exploit its name for his commercial use unless with full subjection and adherence to its rules and principles to say the least.

Therefore, Islamic banks for associating their banking activities with Islam are supposed to fully abide by Shariah rules and uphold at least the cost-free social responsibility, and doing so requires no show of gratitude by Muslims towards these institutions.

Now based on the writer's experience from working for Islamic banks, it can be said that in order for Islamic banks to fulfill that, they must undergo a reform on different levels as shown in the following discussion

What to reform in Islamic banking?

Based on the status quo of Islamic banking, upholding a social responsibility by Islamic banks in the way described above necessitates reforming steps in the following fields.

1.The financed sectors

In this regard Islamic banks should do the following:

- Relaxing the stringent criteria set by Islamic banks to provide financing to the small and medium enterprises, and not favoring the big enterprises in view of their better credit evaluation.
- Selecting financed projects on the basis of their optimal outcomes and their possible contribution to the welfare of the society.
- Investing in the economies of the Muslim and developing countries, not in the economies of the rich countries or in ways that eventually feed their economies.
- Reducing the finance of luxury goods and services and favoring instead the finance of capital goods and assets.
- Restricting the products that normally encourage unnecessary debt incurring like credit cards and personal financing.

2. The internal policies

In this field Islamic banks should do the following:

- Observance of justice when determining fees and fines, since high fees burden clients and may lead to a decision to depart Islamic banks to conventional banks especially after the formers have been already criticized for charging high fees.
- Taking a genuine risk of the financing underlying contracts and not shifting that risk to the financed

clients, as this unlawful practice may unjustly burden clients and impact their ventures.

- Desisting from playing around Shariah rules to snatch unlawful capital and return guarantees from the clients financed on an equity basis. This practice renders the financing conventional in essence and thus leads to the same economic and social evils of Riba.
- Managing the charity fund, which mostly generates from the bank necessary or accidental unlawful earnings, to support some social causes instead of seeking some fatwas to legalize redirecting this fund for the benefit of the bank.

3.The nature of the financing products

Islamic banks can never play a positive role in the society unless they distance themselves from the evils of Riba. However, this will never materialize if Islamic banks persist on seeking legitimacy for their products from adherence only to the technical requirement of contracts. Just like packaging and labeling a bottle of wine in the same way a fruit juice is packaged and labeled will not eliminate the evils of wine, executing a Riba-bearing transaction with the use of some Shariah terms and technicalities will not either change the fact that it is Riba. In fact, Riba was prohibited for its evils and the means used to reach it has no consideration in this prohibition. In the holy Quran we read that some Jews were punished because they persisted on Riba dealings "وأخذهم الربا وقد نهوا عنه" (Quran, 4: 161). However, commentators of the holy Quran mention that their persistence on Riba dealing was indirect; i.e. through apparently valid transactions executed to reach the same end result of Riba.

Therefore, maintaining a sufficient distance from the allure of banking with Riba entails a full departure from all Riba tricks and means, and only then Islamic banks will be able to genuinely uphold social responsibility. This is especially true since taking Riba with one hand and paying some charity with the other will not do society any good. In other words, no matter how benevolent and merciful Islamic banks can be in paying charity or pricing their products they will fail to bring in prosperity to the society if their financing products boil down in reality to conventional.

Thus, it is extremely important for any perceived social role of Islamic banks that the nature of Islamic financing products is void of Riba elements and tricks, since the evils of Riba are powerful enough to outweigh and suppress any good Islamic banking may involve.

Now having identified the nature of the financing products as the most critical element to achieve social good in Islamic banks, this paper comes now to examine the current methodology used for product development in Islamic finance. The purpose of the course is to propose any reform in this methodology if required, so that it eventually leads to having genuine Islamic products whose embedded social good is protected from the evils of Riba and manifested in reality.

II. The basic Shariah requirements in product structuring

For the validity of any transaction Shariah dictates that the underlying contract must fulfill certain conditions. Some of these conditions relate to the contractors, like being eligible to initiate agreements and possessors of the necessary legal capacity. Others relate to the contract itself being independent and unconditional on the occurrence of something else. The subject matter of the contract needs also to be in line with the Shariah, most importantly being permissible itself and meant for permissible use. Having fulfilled all the structural requirements, the contract must also harmonize itself to meet, or at least not to be in conflict with the objectives of Shariah since an apparently valid contract may be misused to reach an evil end, or its implementation may result in causing serious harms and negative impacts on the contractors or the society in general.

Thus, it must be carefully observed that Shariah clearance of products can be legitimately claimed only after two different categories of Shariah requirements have been fulfilled. The first category relates to the structural conditions of the underlying contracts; i.e. the form of the product, while the second category relates to the essence, spirit and implications of the product. Both categories are equally important and essential in product development; however, this equation has not been fully observed in many of the developed products. The balance has been obviously tilted in favor of the first category at the expense of second one as evidenced in the following discussion.

References

1. Many Islamic banks redirect a portion of this fund to their collection department. This has reached in some cases 85% of the fund, excluding the Zakat fund!
2. This Aya means: (and also - the punishment is - for their taking of Riba though they were forbidden from taking it)
3. Ibn Abbass was quoted to have said that they dealt in Riba through manipulation of some sales contracts. Al-Razi, Al-Tafseer Al-Kabeer, V3, p148.

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Part 2

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III. The current methodology used for product development in Islamic Finance

What characterizes the current methodology of product development in Islamic finance in general is not looking beyond the product formal and structural conditions. Although maintaining a proper form is a Shariah requirement, but it is a Shariah requirement also to maintain a proper substance. In fact, a careful study of the literature of Islamic law leads to unveiling the fact that in contracts, the form is meant to protect the substance. In many Fiqh applications, it is noticeable that schools of Islamic law have somehow compromised some aspects of the contract's form but never compromised the contract's essence or spirit. (Abozaid, 2004: 367). This implies that jurists viewed form as something not meant for itself but rather to help protect the essence of contracts and agreements. Some modern practices of Islamic financing product development have implied the opposite; taking care of form and neglecting the substance of the contracts.

The negligence of contract substance is reflected in different practices as in the following:

3.1. Negligence of the contract substance by the deactivation of some contract rules

No doubt that any contracts' rules and conditions are meant to enable the contract to serve its purpose in fulfilling the contractors' needs in a just, positive and productive manner. This explains why contractors in Shariah are not allowed to make personal stipulations that may annul the contract rules (Ibn Qudamah, n.d.: 4/167). Naturally, a contractor, when given an absolute right in making stipulations, will try to turn the scale in his favour even if it is at the expense of the other. However, in some cases we find, especially in uqud al-ez'an (contracts of subjection) where only one party of the contract formulates the contract, that some contracts rules are indirectly neutralized by adjusting some clauses or incorporating new ones as in the following example.

Example: Ijarah Muntahia Bittamlik

Being a contract of lease, Ijarah Muntahia Bittamlik in the Islamic banking application is supposed to fulfill the following basic Shariah structural conditions:

- The leased asset requested for financing is valuable from Shariah perspective and not declared by the client to be used for Haram purposes. This would exclude for example financing clients in acquiring machineries that process tobacco products.
- The leased asset is clearly identified by the parties, and the rent is specified in the contract. If there is gharar (uncertainty) in the contract, then it must be minor since the major gharar invalidates the contract.
- The leased property remains in the ownership of the lessor for the duration of the Ijarah period, and then it is transferred to the lessee by virtue of a completely independent contract, like sale or gift.
- The bank, as lessor, bears all liabilities related to ownership, like property taxes and major maintenance required for keeping the asset valid for use by the client.
- The lease period commences from the date on which the leased asset has been delivered to the lessee.

These are the basic rules of Ijarah Muntahia Bittamlik, and a theoretical investigation of any of its contracts in Islamic banks will prove consistency and full abidance. However, some apparently-valid clauses are added to this contract, leading to the deactivation of some of these basic rules and thus to the negligence and distortion of the Ijarah essence. One clause relates to the division of lease rental into three elements: fixed, variable and complementary. The problem, however, lies with the complementary and to a certain extent with the variable rent. The complementary rent represents any cost the bank as owner has incurred in the past Ijarah period. The cost includes taxes, insurance and major maintenance expenses. Although these are supposedly the responsibility of the bank as an owner, the bank after paying them claims the same back from the client under this clause by adding it up to the next Ijarah rental.

Obviously this paralyzes the in-contract Shariah rules pertaining to the liability of the owner in Ijarah for the property risks and renders it ineffective. In fact, this practice of effectively shifting property risks to the lessee is especially critical in the application of Ijarah Muntahia Bittamlik since it brings this financing instrument closer to conventional financing after removing the justification for profiting which is based on the notion of "al-Kharaj bid Daman" (liability justifies the gain). The core difference between Riba and trade remains the risk taking which is normally associated with trade. This risk taking is totally eliminated when the bank indirectly shifts the leased property liabilities to the client, and even in case of property partial or total damage, it is the client who bears it as he is the one who effectively pays the insurance premiums.

On the other hand, the problem with the variable element of Ijarah rental relates to the uncertainty this practice involves. Banks tie this element to an interest rate benchmark like LIBOR. The problem starts when banks do set and cap only one end of this excessively volatile benchmark, i.e. its floor. However, a ceiling needs also to be set and capped at a certain figure in order to minimize the gharar then involved and thus maintain the validity of the contract. Nevertheless, banks tend to only protect themselves from the undesirable movements of the benchmark by capping the minimum amounts payable by their clients and have no desire to cap the maximum amounts payable by their clients. This practice creates excessive gharar and opposes the Shariah requirement to determine the lease rental in any Ijarah contract.

Moreover, the above deviation from Ijarah Muntahia Bittamlik rules manifests itself more blatantly when the asset leased in Ijarah Muntahia Bittamlik originates from the same client. A client who needs cash or refinancing will be instructed by the bank to sell to it an asset or a common share thereof, then to lease it back from the bank through Ijarah Muntahia Bittamlik. The bank frees itself from all asset liability in the manner described above and the client repays with a markup the financed amount in the form of rentals. This transaction has been widely used recently to enable banks to restructure non-performing debts in the wake of the financial crisis.

Thus, we see how the same clause in one contract can be neutralized by another, leading eventually to the distortion of contract substance and thus stripping the contract of its Shariah spirit and objective. Although Islamic finance has developed Ijarah contract into a new model and helped maintain most Ijarah rules in this creative instrument, it has however left a room for individual Islamic banks to twist the substance of the contract and deprive it of its nature as a lease contract.

3.2. Negligence of the contract substance by attaching another contract

Contracts of financial transactions in the Shariah are meant to fulfill the various needs of contractors, like acquiring an asset, acquiring an asset's usufruct, investment of capital and delegation of authority. However, it can be observed that some of these contracts are driven totally out of their objective when they are predetermined to be followed by other reversing contracts.

Murabaha , which is a sale contract originally designed in its banking application to finance clients in their acquisition of assets, is used for a different objective altogether. It is used to provide clients with cash money through colluding to sell them assets on Murabaha basis then to sell the same assets on their behalf in the market for cash price. Clients get the desired cash and remain indebted to the bank for the Murabaha deferred price. Here we have two independent sale contracts each of them is lawful in itself but the end result of executing them consecutively is a cash financing technique which is effectively no different from conventional cash financing. Obviously, the result of this transaction is against the substance of the Murabaha sale contract. Murabaha in this transaction does not lead to real holding of asset ownership by the client. This is a deviation from the objective and substance of Murabaha, which is a commodity financing instrument that helps clients own their desired assets.

3.3. Negligence of the contract substance by the misapplication of the contract

Contemporary collective fatwas have helped structure many products that are essential for the operation of Islamic financial institutions. However, the application of some of these products may have deviated from what they were originally designed for. A good example would be using for speculation what was designed for hedging.

Islamic finance has developed certain tools to hedge against some inevitable excessive market risks. These tools include unilateral binding promises and tools whose underlying contracts are Salam contract and Urbun sale. Now, apart from the Shariah debate over the validity of these tools to be used as hedging instruments in contemporary Islamic finance or Islamic capital market, some of these tools have been misapplied and used for speculation as well, although speculation was considered an invalid domain in what is known as "Islamic derivatives".

Recently one Islamic financial institution has offered a product whose structure is basically as follows: The client opens a designated investment account with the bank. The bank operates the designated account in its capacity as investment manager. The Investment Manager then uses the amount deposited in the said account to purchase Shariah compliant assets at some prevailing market prices. In most cases the assets will be shares selected from an Islamic stock index.

The client gives a unilateral promise to the bank to sell the shares at a predefined price called the "Settlement Price". The bank in return gives a unilateral promise to the client to buy the shares at the Settlement Price.

The settlement price relates to the performance of some specified underlying reference asset (the "Reference Asset", which could be an index) rather than the performance of the Shares in the Islamic Account. Thus, two scenarios are perceived:

Scenario I: The value of the relevant shares goes up more than the performance of the Reference Asset. In this case, the bank can purchase the relevant Shares from the client at a price lower than the market value for such shares at that time. Thus, the bank would hold the client to his promise, while the client would not be interested in holding the bank to its promise as selling the shares at a value which is lower than the market value at that time would incur a loss.

Scenario II: The value of the relevant shares goes less than the performance of the Reference Asset. In this case, the bank can purchase the relevant shares from the client at a price higher than the market value of such shares at that time. Naturally, the bank in this case would not be interested in holding the client to his promise while the latter would hold the bank to its promise as he can then sell the relevant shares at a value higher than the market value for such shares at that time.

Therefore, in both scenarios noted above the client will sell the relevant shares to the bank for the settlement price as agreed on the basis of the performance of the reference asset. This sale is certain as it will serve the interest of either the bank or the client. The certainty of this sale makes the mutual promise to execute the sale binding on both parties and thus the promise will be tantamount to a forward sale contract, which is a breach of Shariah laws of sale contract.

Obviously the substance of this transaction is hardly distinguishable from that of any conventional derivative with the speculative element embedded therein; both contractors are speculating on the movement of the value of the reference asset, which is mostly an index. It is very likely that such a structure may even develop to involve financing the client to purchase the shares, then settling the deal with the loser of the two parties paying the price difference to the other.

In conclusion, this transaction involves a misapplication of promise which can originally function as a hedging tool for risk mitigation

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1. This type of Ijarah is not found in classical books of Fiqh; it is a creation of modern day jurists. It comprises two different contracts: contract of leasing (ijarah), and contract of sale. (bay'). The bank promises the client that upon the successful completion of the Ijarah, the bank will sell the asset to the client at a nominal price or will gift it to him.
2. These detailed Shariah rules can be sourced from main Fiqh books like Al-Shafi'i. Al-Um, 3/14; Ibn Abedeen. Hashiyat (Rad al-Mukhtar ala al-Dur al-Mukhtar) 4/88; Al-Kasani. Badai' Al-Sanai' 5/67; 6/71; Al-Bahuti. Kashaf Al-Qina', 3/53; Al-Dasuqi, Hashiyah 3/143.
3. "Al-Kharaj bid Daman" is originally a Hadith narrated from the prophet (peace be upon him); however, it was recorded as a Fiqh maxim by Al-Soyoti in his "Al-Ashbah Wal Naza'ir", p 154.
4. Murabaha in the banking application refers to a sale contract preceded by an agreement with the client to buy the desired commodity from its supplier then to sell it to the client at the cost plus a markup (Ribh).
5. Salam is the sale of future delivered goods against upfront paid price.
6. Urbun is a sale with the condition that the buyer has the right to revoke the agreement in return of forfeiting the advanced down payment, which is called urbun. If, however, the sale is concluded, then the urbun advanced is deemed as part of the price.

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IV.Reasons for neglecting the contract's substance in some Islamic financing products

A direct examination of the Islamic banking market conditions, challenges and products identifies the following reasons for any deviation from the true rules of Sharia.

4.1. The desire to offer the same financing facilities of conventional banks

Conventional Islamic banks treat money as commodity, therefore they have no problem in providing cash financing to clients with profit. This cash financing can take the form of personal loans, overdraft facility or refinancing, all through interest-bearing loans. However, since lending money on interest is haram, the Islamic banks willing to offer these profitable financing facilities had to design certain products that would serve such purposes. Logically, the designed products would necessarily lose Shariah spirit and breach contracts essence because they are basically meant to fulfill unlawful objectives, i.e. profiting from providing cash to clients. The structured products relied on bogus operations of selling and buying commodities, using mostly the highly controversial eina and tawarruq sales as their underlying contracts. (Abozaid, 2004) . In fact, sale contract is designed to help people acquire commodities for their own use or to resell them and make a profit, but it is not designed to justify unlawful dealing in cash by buying expensive and selling cheap simultaneously. This is a deviation from the purpose of the sale contract and a defeat of the purpose behind Riba prohibition. If engaging in cash financing with a mark-up through the technicalities of sale contracts like eina or tawarruq is halal, then the whole purpose behind Riba prohibition will be defeated. Any two willing to deal in loans with a return would simply do so through eina or tawarruq- like sale contract, the end result being exactly the same.

4.2.The unwillingness to bear genuine property/ contracts risks

Being financial institutions, Islamic banks tend to avoid as much as possible the risk that is normally embedded in the Shariah contracts used in product structuring. This avoidance of risk may lead to depriving contracts of their Shariah identity and rendering them spiritless. The application of Ijarah Muntahia Bittamlik in the manner described earlier is an example. The liability risk related to the ownership of the leased asset is effectively transferred from the bank to the client and thus the essence of the lease contract is distorted. Murabaha is another example when the bank frees itself from the Murabaha commodity liabilities. Neglecting the sale essence in Murabaha product is at its peak when the Murabaha client is appointed as the bank's agent to buy the commodity from its supplier, take delivery then deliver to himself, without the bank being responsible for even commodity defects or claim. In this scenario the bank's role is limited to only advance of money to the property supplier, thus mimicking the limited role of conventional banks.

4.3. Legal constraints facing the right application of Shariah rules in products

In some countries the legal system stands as a stumbling block to the proper application of Shariah rules required for product structuring in Islamic

finance. Some Islamic banks for example find it inescapable to make the purchase appear in the client's name, because according to some laws, banks are not allowed to trade in assets. Others are prohibited from leasing assets to clients and therefore they are left with no choice but to dodge and execute Ijarah in the form of sale. Imposing high taxes on registration of assets purchased is also a legal constraint as it eventually leads to increasing costs on clients when banks are commanded by law to register in their names what they buy before they sell to clients. Some banks tend to avoid payment of high taxes by reducing some necessary contractual steps or faking some contracts.

Are these reasons justifiable?

No doubt that legal constraints can justify some leniency and indulgence when necessary; however, Islamic banks have no excuse to follow the example of conventional banking offering the same products regardless of whether a particular product is Islamizable in spirit or not. Islamic banks have to acknowledge the fact that not all conventional products can be Islamized, and that any attempt to this effect will yield nothing but a product borrowing its legitimacy from adherence to mere technicalities and meaningless structures. The avoidance of inherent risks to the degree of twisting contracts and deforming their nature is not justifiable either. In fact, it is necessary for Islamic banks to note that they become distinguished from conventional banks only when they genuinely submit to Shariah rules and maintain the nature and essence of Shariah contracts. The mere maintenance of contracts technicalities and terminologies does not render contracts in compliance with the Shariah rules. This issue is particularly important since Islamic banking derives its credibility from the declared full adherence to Shariah rules; therefore, compromising this notion, unless it is extremely necessary, is never justifiable.

V. Conclusion: The proper methodology needed for product development

It has become obvious from the past discussions that for a proper structuring of a product under Islamic finance, three aspects of the product must be well taken care of.

First is form, and form relates to fulfilling the Shariah basic structural requirements and conditions of contract and contractors. A contract whose form is invalid produces no legal consequences and can be considered as null and void.

Second is substance, and it is concerned with the essence and the spirit of the structured product, especially when more than one contract or element is involved in the product, since this may yield a controversial product as is the case with eina or tawarruq. Two sale contracts are involved herein, each is independently valid in essence, but the total outcome of having them consecutively executed is a highly controversial cash financing product.

Third is the implication of the structured product that has passed the form and substance test. The structured product must not lead to evil or have unfavorable or negative implications. Just like selling weapons to a criminal, or grapes to a wine maker, does not comply with Shariah although the contract itself may have fulfilled all of its structural conditions, an Islamic banking product cannot be truly labeled Shariah compliant unless it is free from evil implications. For example, in the absence of sufficient controlling measures on shares trading in the stock market, this market can become an arena for gambling and zero-sum games; therefore, developing a financing product that helps finance clients willing to participate in such market becomes haram, although the product itself may be sound in its structure and essence.

In other words, for a product to be truly labeled as Shariah compliant the underlying contract and tools used in its structuring and developing must be valid in form and essence, and the usage and implementation of the developed product must also be in line with the Shariah rules and principles. Reexamination of the current Islamic banking and finance products in light of this elaborated benchmark is deemed extremely necessary, since there exist among the current Islamic banking products ones which have successfully fulfilled the Shariah requirements in terms of form, but unfortunately failed to fulfill that of substance or implications. Unless Islamic banks review their products and reform them to meet the criteria of this proposed methodology, Islamic banks' role in achieving the social good will remain very limited if not overwhelmed by the evils of their Riba-like transactions.

On a final note, the recent trend of distinction in product development between a Shariah compliant product and a Shariah based product is inaccurate and lacking Shariah bearing. What complies with the Shariah is only what is halal, and a contract that is structurally valid but eventually leading to an unlawful end can never be regarded as halal. In other

words, when we say that something is Shariah compliant, it means that it fits within the Shariah rules and principles. But how would a product that carries the same economic evils of Riba or gambling fit within a Shariah set of rules and principles even if it has a valid structure!?

If a distinction is ever made in Shariah contracts acceptability, then it is the juristic distinction between the two legal terms within the framework of Islamic law: valid and permissible. A valid contract is the one that has a valid form regardless of the validity of its purpose or the contractors' intention. Conversely, a permissible contract is the one that has a valid form, purpose and objective. Obviously, a valid contract is not necessarily permissible since a contract can be structurally valid but it is conducive to evil or meant by contractors to reach an unlawful end, like selling weapons to a criminal or executing a series of sales to legalize Riba as in eina. This distinction between valid and permissible corresponds in fact to the issue of form, essence and implication of contracts. "Valid" relates to form, while "permissible" according to all schools of Islamic law relates to contract essence, implication and intentions of the contractors.

Therefore, a contract is acceptable to Sharia, or is complying with the Sharia, only if it is valid and permissible, since both concepts are necessary elements of Shariah clearance, and Shariah does not admit a contact or a structure that is invalid in essence or implications.

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2. This is based on the well-known Fiqh maxim "العبرة في العقود للمقاصد والمعاني لا للألفاظ والمباني" (Contracts are judged by their essence and meaning, not by their form and structure) which is originally derived from the famous Hadith "إنما الأعمال بالنيات" (matters are determined by intention). This Hadith was narrated by Omar bin Al-khattab (ra). See Sahih al-Bokhari, 1/3, Hadith No (1); Sahih Muslim, 3/1515, Hadith No (1907)-); Ibn Nujaim, Zainulddin, Al-Ashbah Wal Naza'ir, 1/34; Al-Seyoti, Jalaulddin, Al-Ashbah Wal Naza'ir, p.21; Al-Kurdi, Ahmad. Al-Madkhil Al-Fiqhi, p.33.

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