

Islamic Finance Review

ISFIRE

Volume 2 • Issue 1 • February 2012 • £20

Epistemology
of Finance: An
Ideal Islamic
Financial System

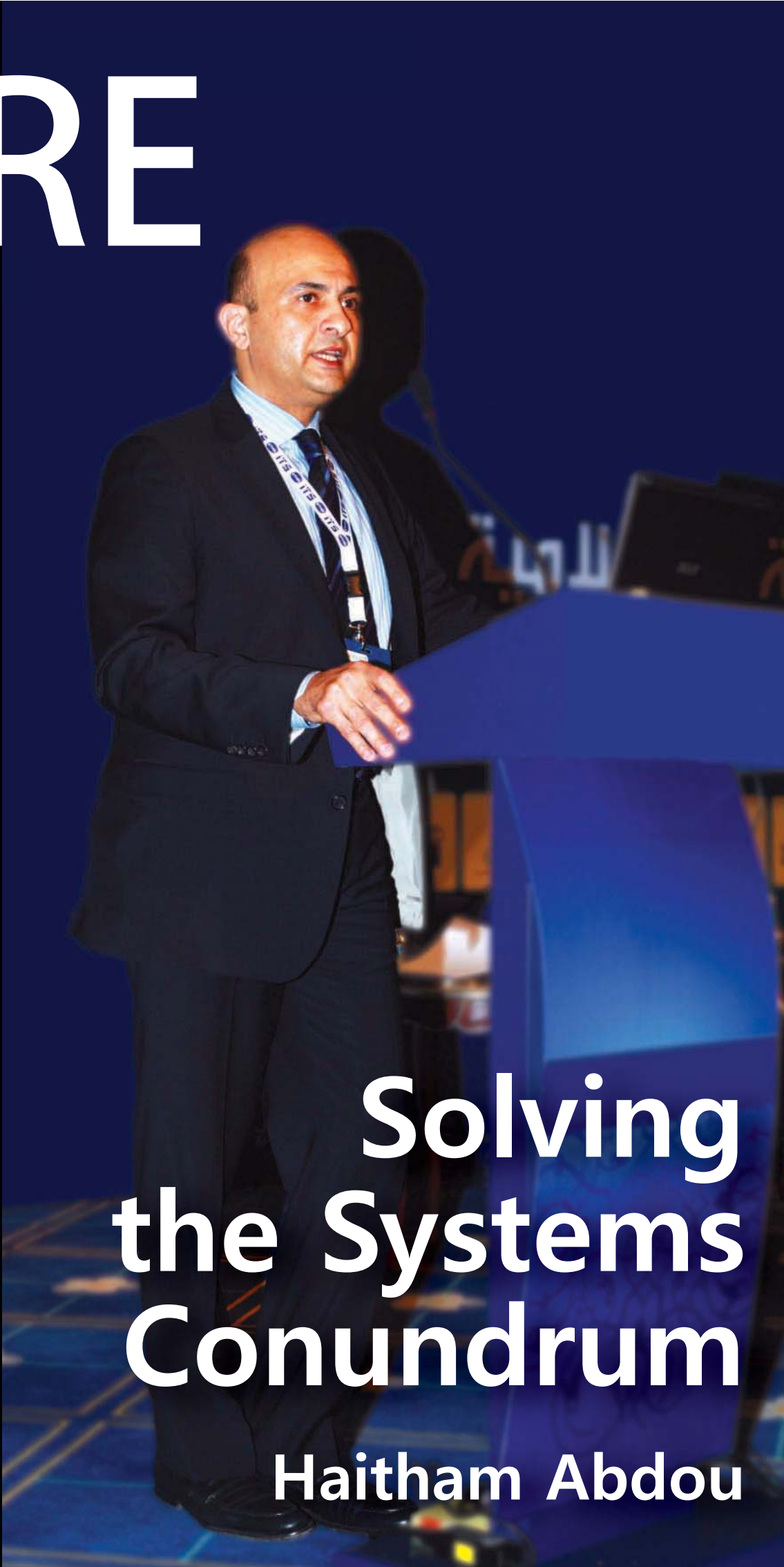
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The wisdom of Oliver Agha

Agha & Co/Agha & Shamsi are currently the only fully fledged Shari'a compliant law firms in the world, headed by the impassioned Oliver Agha. A man of principles and with a higher purpose, Oliver Agha is trailblazing a path within Islamic finance. In this exclusive interview, he takes out time from his busy schedule to discuss his world and Islamic finance.

How do you see the Islamic finance industry developing in the next ten years?

Generally, along positive lines. I predict that there will be a concerted move towards an examination of the core spiritual principles that underlie the practice and a move towards making structures more congruous with a spiritual mandate inherent in the Judaeo/Christian/Islamic ethical ethos. There will be more concentration placed on developing the correct structures, displacing those built on erroneous foundations and developing and strengthening the regulatory framework, which is in need of significant development. There will also be an exponential increase in Islamic scholarship. On balance, I view the next decade as an intellectual and spiritual renaissance resulting in re-examination with development of genuine products direly needed by the hungry populace.

Islamic banking will also serve as a stabilising force in the global economic order. The financial crisis of the past few years has led to an increased awareness of the problems with conventional banking. The crisis has led to enhanced regulatory attention and plans to control 'risk' in the conventional banks. The 'risk' in these systems is multiplied by the very nature of fractional reserve banking, which gives conventional banks the discretion and power to simply create or eliminate credit, albeit subject to apparently stringent rules. For example, when asset prices increase at a fast pace, conventional banks seize the opportunity by granting more credit

backed by inflated assets, which is problematic. Deposits in Islamic banks (which are not loans but true investment deposits on a mudaraba basis), however, are re-invested in the real economy to create new flows of goods and services without any artificial money expansion. The 'choking' of credit and its devastation on the economic system has highlighted the fragility and inherent weakness in the interest bearing debt-based financial system. These factors should result in a closer look at the equity based constructs that are a mainstay in the Islamic system and one more reason that should spur the development of Islamic finance.

Are there enough lawyers in the Islamic finance industry who have a thorough understanding of both Islamic law and western law, be it common or civil?

No. Most lawyers that are practitioners do not appear to have grounding in Islamic jurisprudence. This lack of grounding in the field of law in which they practice is unique to Islamic finance as a practice area. If I were a tax lawyer in the US or a securities lawyer, I would need to be well-versed in the Tax Code or the Securities Acts, respectively. However, no such competence is made requisite in firms for Islamic finance practitioners.

What are the challenges fac-

ing the Islamic finance industry and what needs to be done to overcome them?

There are serious challenges facing the Islamic finance industry. Islamic finance is beset with credibility problems. Many cannot differentiate between conventional and Islamic products; some of this is unfair and due to a lack of understanding of the actual risk profile (e.g., in an ijara finance the financier assumes risk of loss which is markedly different than that in a conventional mortgage situation where the mortgagee (bank) does not); however, in other products such criticism is well-founded. In some cases, certain Shari'a structures have been approved that make little legal or commercial sense – this posits serious enforceability issues. Legal and Regulatory frameworks in countries are severely deficient and do not provide a framework for the fluidity required for efficacious transactions; nor does the system envisage a requisite Islamic dispute resolution system with concomitant procedures and laws – Islamic finance is not understood and in some instances (and in Islamic jurisdictions) is not treated even on par with conventional finance. For example, there are mortgage laws that protect conventional mortgagors but no mechanism for Islamic ijara financiers to quickly exercise their rights against a defaulting ijara lessee – this exercise gets stuck in a system that does not know what to make of the litigants. This sort of regulatory vacuum – gap in understanding of Islamic finance structures at the judicial and regulatory



levels - threatens the proper development of Islamic finance risking some Islamic financiers getting fed-up and moving on or reverting to the tried and tested conventional system. At the governmental levels, similar problems exist as there is confusion across the board on how to record the legal interests of Islamic obligors e.g., the Islamic financier/owner vis-a-vis the customer/lessee and designated eventual owner. There is a dearth of human capital – many of the non-Muslim practitioners in the field have little understanding of Islam or Islamic law. For example, Islamic finance is the only field of law where lawyers that have no training in Islamic theology and jurisprudence hold themselves out to be “Islamic finance lawyers.” Conventional bankers largely seem enthused about the market opportunity which exists but, again, and understandably so, without a due appreciation for the spiritual principles that underlie Islamic finance. When you go through the actual state of the Islamic finance market, it is a wonder that it has survived at all; in fact, it continues to grow despite the endemic and extraneous pressures. In sum, Islamic finance has grown despite the mistakes and imperfections of the practitioners.

What is your opinion on the form vs. substance debate?

As noted above, Islamic finance is in a struggle for its soul. It must break free of the temptation to take the path of replicating conventional products. Success on the material plane by sacrificing its spiritual mandate is an actual failure from an Islamic perspective. The goal of Islamic finance is not to achieve market success by replicating conventional products in Islamic garb but by the development of an alternate, and co-existing system, based on equity and quasi-equity variants that envisage conducting business tempered by spiritual considerations.

Do the multiple opinions in Islamic law act as a hindrance to the global growth of the industry? Is there a need for standardisation or can Islamic finance succeed with having differences of opinion?

Generally, it is difficult to ‘impose’ one view on disparate adherents across the globe. However, there can be a general consensus on certain core commercial matters and the standards promulgated by AAOIFI, while neither perfect nor necessarily adequate, are a good start. Islamic fi-

nance has been growing despite all the problems noted above so any conformity in relation to core principles for products would be only helpful.

Regulation is important in supporting and promoting Islamic finance. For the ongoing success of Islamic finance, is it necessary to islamise a regulatory system – like Iran - or adopt a dual model – such as Malaysia? Which model do you think is best?

Islamic finance exists in a world where the norms are conventional systems. Countries that are open to developing Islamic finance need to establish dual models enabling Islamic finance to co-exist with the conventional systems. Let there be choice and let the market decide whether to invest/partake in interest based or risk-sharing approaches.

Tell us a bit about Agha & Co/Agha & Shamsi.

The firms are law firms established with the mandate of representing clients on permissible transactions. Our Shari’a board, like the board of other Islamic entities, delineates our mandate in respect of acceptable clients and representations. Generally, we cannot represent conventional banks in their conventional transactions, enforcement of interest bearing debt matters, or clients for gaming projects (casinos), alcohol or tobacco manufacturers. We cannot avail of debt facilities to pay our partners or employees. There are currently 17 persons working with the firms.

The most novel transaction that we have worked on to date involved a variation of a diminishing musharaka and murabaha structure that best approached the commercial requirements without treading on Shari’a concerns. We have also structured with Shari’a scholars and documented intricate Shari’a structures effecting portfolio sales of leased assets and developed commercially viable and Shari’a compliant structures for takaful operators. We also work regularly with leading Islamic financiers in litigating Islamic ijara disputes and defending or asserting Shari’a arguments in such cases. I also serve as an independent expert witness in Islamic fi-

nance disputes.

Please explain the difference between Agha & Co and Agha & Shamsi and the relationship between the two?

The two law firms are affiliated legal entities. Each has been set up to comply with the regulatory requirements of each Emirate.

Where are most of your clients based?

Our clients are based in the UAE, Saudi Arabia and the United States. US and Western clients find it culturally familiar to work with us since many of our lawyers have had large US/International law firm backgrounds and top tier credentials, and the firm follows the ethos of a NY or London firm with a same day response time, where possible.

What transactions and kind of work do you commonly work upon?

Since we represent, among other clients, three of the leading Islamic mortgage financiers, DGF (Deutsche Bank’s Saudi mortgage finance entity), Tamweel (UAE’s largest Islamic mortgage financier) and Amlak, our practice in Ijara financing and dispute resolution practices are our flagships. In addition, we work with leading corporates on cross-border M&A deals, joint ventures or on cross-border projects with complex EPC and project contracts.

How do you define success – working on the largest Islamic finance transactions or the most genuine ones?

Of course we would be enthused to work with large Islamic finance transactions. However, these deals usually go to some of the largest, global firms. We are quite capable of handling these (and have the back-up of a large and quality firm, Pillsbury, in any case). However, to the extent these deals replicate conventional profiles or raise the ire of our Shari’a board we would not be comfortable in working with such deals. Therefore, we satisfy ourselves in working with smaller deals that have a more genuine spiritual underpinning.

Who are your competitors? How does Agha & Co/Agha & Shamsi differ from the major players in Islamic fi-

nance such as Clifford Chance, Norton Rose and other large commercial law firms?

Our competitors are the large law firms. As alluded to before, we differ from these firms in that we cannot represent conventional clients generally or clients involved in impermissible transactions. Additionally, we have a Shari'a board. We are unique, as being established as a Shari'a compliant firm, and being able to issue legal opinions on Islamic law. This is an important niche as we see there being a real gap in the market in this area that we can fill in while working co-operatively with other firms.

What are your plans for Agha & Co/Agha & Shamsi and where do you wish to take it the firm? Do you wish to expand the firm outside the UAE?

The vision for the firms is to deliver excellence in the practice of law while staying true to its ethical mandate and circumscribed practice areas. Growth is considered, to the extent there is a business case. We currently are working with clients in Saudi Arabia, Qatar and Oman.

What influenced you to start up a Shari'a compliant firm?

I started up a Shari'a compliant firm in order to reflect spiritual goals in the workplace. While there are Islamic banks takaful companies, there were no Islamic law firms. Naturally, I knew that beginning a Shari'a compliant firm would entail giving up the lion's share of my clients that were conventional financiers and there was fear that there would not be enough business to survive. However, we have managed to get by, one day at a time, and are commencing our fourth year, by the grace of the higher power.

How would you compare working within a large commercial law with working in a niche law firm which focuses on Islamic finance?

These are very different experiences. Working in a large law firm is akin to being on a large cruise ship. It is very



comfortable, generally. However, you have to be comfortable with the destination towards which the ship is headed. A small firm is a smaller vessel – more adept at making quick turns and with more freedom of choosing its destination.

Take us through an average day in the working life of Oliver Agha.

An average day involves going to work, client matter attention, work on firm and client development matters, attendance at weekly firm education seminars, work with AAOIFI (I sit on their board) and WIFI (recently established European Islamic body to aid in the development of the Islamic finance industry) and if I am lucky, getting to the gym.

What do you do when you are not working?

My interest is the study of comparative theology; so I spend time reading different religions' approaches. I have found the Talmud and the Torah to be particularly interesting and rewarding. One of the pearls of wisdom from the Torah I have acquired notes "Fools believe that the money which they have lying in their coffers is theirs, while the money they give away to charity is theirs no longer. Actually, quite the reverse is true. Only those possessions which are given away for sacred purposes remain one's property ("each shall retain his sacred donation," Num. 5:10). But the possessions which a man greedily amasses for himself are not his at all. Such gains will

not remain with him for longer than a fleeting moment." CHASIDIC [27]. The Union of American Hebrew Congregations, *The Torah: A Modern Commentary*, 1056 (W. Gunther Plaut ed., Jewish Publication Society 1981) (1962).

Tell us a bit about Oliver Agha. Where did you study? Where have you worked?

I went to high school in the US (in Scarsdale, New York), then went to New York University and after having worked in the corporate world for a few years, went back to law school (New York Law School). I worked, among others, at Fulbright & Jaworski LLP in the US, India, Hong Kong and Beijing (for about eight years) and then moved to Clifford Chance's Saudi affiliate where I headed the Projects department and co-headed the Islamic practice. At that time, I became involved in some of the large Islamic deals in the region. Subsequently, I joined DLA Piper in Dubai before launching Agha & Shamsi in Abu Dhabi and Agha & Co in Dubai.

What is it about Islamic finance that impresses you?

The spiritual message in Islamic finance is most rewarding. For the idealist in me, it posits a society where partnerships and partnership structures are commonplace and commerce and transactions are infused with an ethical perspective.