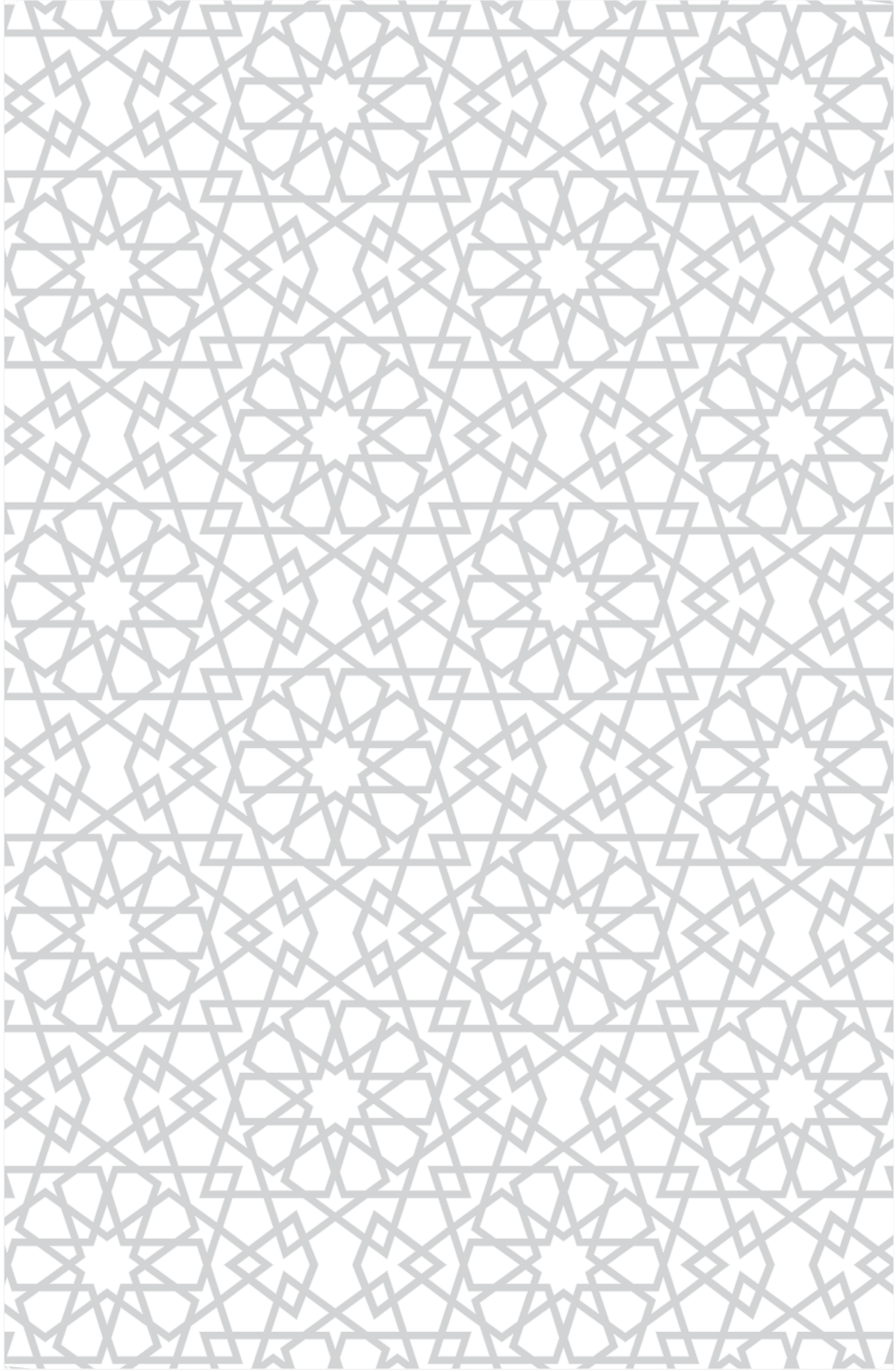


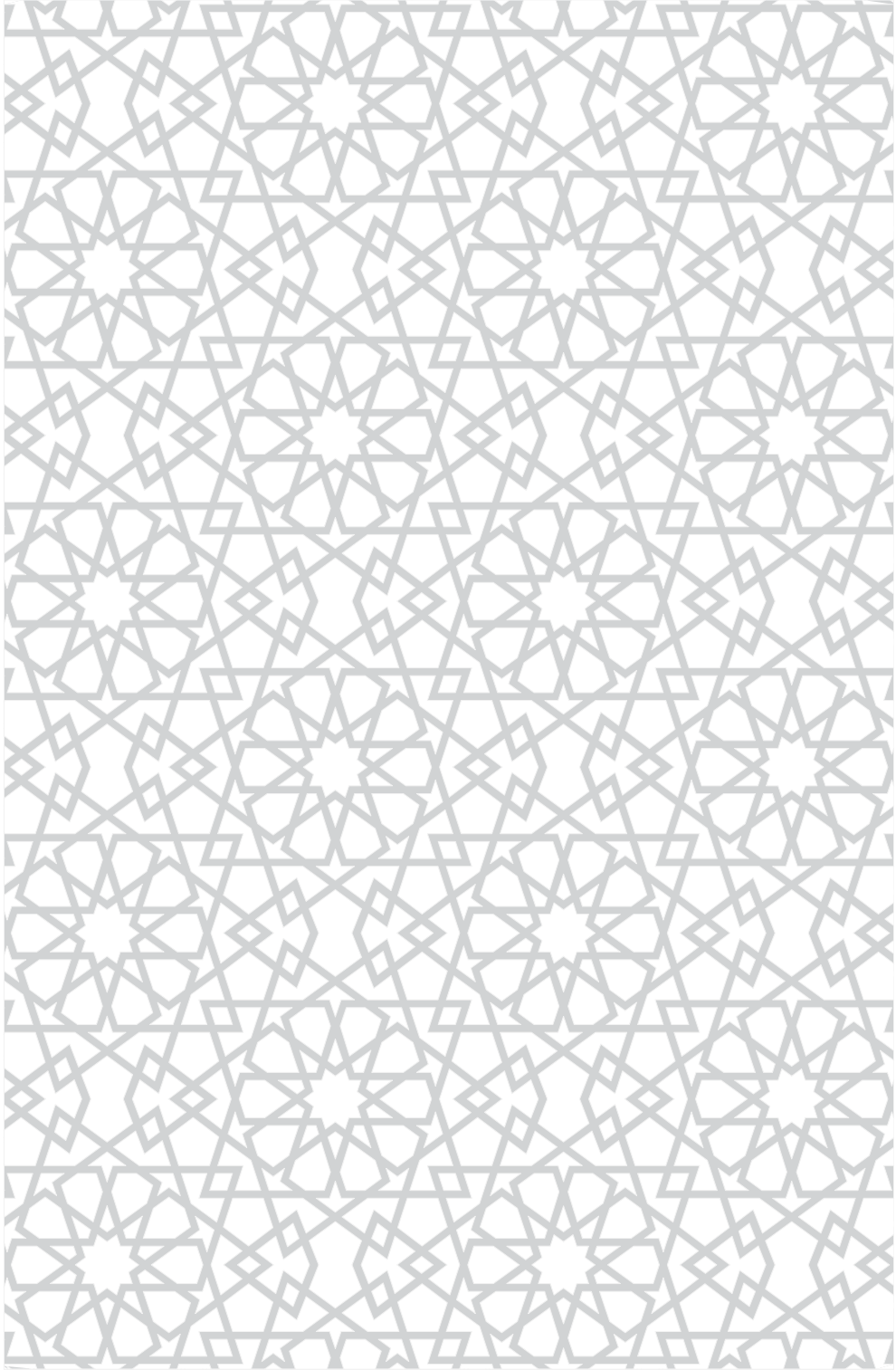
Shari'ah Standard No. (5)

Guarantees
(Revised Standard)



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IN THE NAME OF ALLAH, THE ALL-MERCIFUL, THE MOST MERCIFUL

All praise be to Allah, the Lord of all the worlds, and blessings and peace be upon our master, Muhammad, and his household and all his companions

Preface

The aim of this standard is to outline the Shari'ah rules governing guarantees, and to clarify the forms of guarantees that are permissible or prohibited. It also outlines some significant modern applications of guarantees as employed by Islamic financial Institutions (Institution/Institutions).⁽¹⁾

(1) The word (Institution/Institutions) is used here to refer, in short, to Islamic financial institutions including Islamic Banks.

Statement of the Standard

1. Scope of the Standard

This standard covers securities (Guarantees) intended to secure obligations and protect debts against procrastination and default. Such securities may take the form of written documents, attestations, personal guarantees, mortgages, cheques and promissory notes. The standard also explains the permissible and prohibited forms of securities. It also intends to distinguish between liabilities and the assets held on trust.

The standard does not cover guarantees against torts.

2. General Rulings on Guarantees

2/1 Permissibility of guarantees and their relevance to contracts

2/1/1 A contract of guarantee is permissible in contracts of exchange, e.g. a contract of sale, or contract of rights, e.g. right of intellectual property. Such a guarantee contract does not affect the permissibility of the original contract in which it is required. It is, moreover, permissible to stipulate a guarantee into the body of an original at one time, because guarantee is appropriate to, or relevant in, contracts.

2/1/2 There is no objection in Shari'ah to include a number of guarantees in one contract, such as incorporating a personal guarantee together with a mortgage of security in the same contract.

2/2 Guarantees in trust (fiduciary) contracts

2/2/1 It is not permissible to stipulate in trust (fiduciary) contracts, e.g. agency contracts or contracts of deposits, that a personal guarantee or mortgage of security be produced, because such a stipulation is against the nature of trust (fiduciary) contracts, unless such a stipulation is intended to cover cases of miscon-

duct, negligence or breach of conditions or stipulations. The prohibition against seeking a guarantee in trust contracts is more stringent in Musharakah and Mudarabah contracts, since it is not permitted to require from a manager in the Mudarabah or the Musharakah contract or an investment agent or one of the partners in these contracts to guarantee the capital, or to promise a guaranteed profit. Moreover, it is not permissible for these contracts to be marketed or operated as a guaranteed investment.

2/2/2 It is not permissible to combine agency and personal guarantees in one contract at the same time (i.e. the same party acting in the capacity of an agent on one hand and acting as a guarantor on the other hand), because such a combination conflicts with the nature of these contracts. In addition, a guarantee given by a party acting as an agent in respect of an investment turns the transaction into an interest-based loan, since the capital of the investment is guaranteed in addition to the proceeds of the investment, (i.e. as though the investment agent had taken a loan and repaid it with an additional sum which is tantamount to Riba). But if a guarantee is not stipulated in the agency contract and the agent voluntarily provides a guarantee to his clients independently of the agency contract, the agent becomes a guarantor in a different capacity from that of agent. In this case, such an agent will remain liable as guarantor even if he is discharged from acting as agent.

2/3 Guaranteeing existing leased properties

The lessor bears the risk associated with the leased property and the lessee holds it on a trust basis. Hence, it is not permissible for the lessor to stipulate in the lease contract that the lessee provide a guarantee or mortgage of security, etc., so that he may use it to recover the amount of the lease rental if the leased property is damaged, unless such a stipulation is restricted to cases of misconduct, negligence or breach of contract. Therefore, the lessor is liable for the consequences of any damage to the leased property that is not caused

by the misconduct or negligence of the lessee, and is responsible for any related insurance expenses. The lessor also bears the expense of any major maintenance work required to keep the leased property in the condition necessary to provide the contractual benefits under the lease.

2/4 Written documentation and attestation

2/4/1 Documentation in writing is recommended by Shari'ah, whether such documentation is in the form of ordinary (private) or official documents. However, customary practice is applicable in the drawing up of such documents and in determining the documents that are relevant as proof (or have evidential value). It is prohibited to forge documents or to conceal their contents or to destroy them so as to bring about the loss of other peoples' rights.

2/4/2 Attestation in financial transactions is recommended by Shari'ah. It is also commendable, and in case of necessity it is obligatory, to give testimony. On the other hand, perjury is prohibited and is one of the major sins.

2/4/3 It is not permitted to scribe or witness acts prohibited by Shari'ah, such as certifying or witnessing borrowing on the basis of interest.

3. Personal Guarantees

3/1 Permissibility and types of personal guarantee

3/1/1 It is permissible for an Institution to stipulate that a customer should provide one or more guarantors to secure the debts owed by the customer.

3/1/2 Personal guarantees are divided into two types. One type is a guarantee where the guarantor has a right of recourse to the debtor, and this guarantee is offered at the request or with the consent of the debtor. The other type is a non-recourse guarantee, which is offered voluntarily by a third party without the debtor's request or consent (voluntary guarantee).

3/1/3 An Institution is not entitled to guarantee financial commitments without a right of recourse to the debtor, i.e. to be a non-recourse guarantor, unless the Institution is already authorised by its shareholders and investors to make donations or to perform acts of benevolence.

3/1/4 It is permissible to fix the duration of a personal guarantee. It is also permissible to set a ceiling on the amount to be guaranteed and it is permissible that the personal guarantee be restricted by, or be contingent upon, a condition. In addition, it is permissible that such a guarantee be made contingent upon a future event, for example, by fixing a future date at which liability will commence and, in this case, the guarantor may validly withdraw the guarantee, by notifying the creditor, before the prospective obligation to be guaranteed arises.

3/1/5 It is not permissible to take any remuneration whatsoever for providing a personal guarantee per se, or to pay commission for obtaining such a guarantee. The guarantor is, however, entitled to claim any expenses actually incurred during the period of a personal guarantee, and the Institution is not obliged to inquire as to how the guarantee produced has been obtained by the customer. [see item 7/1/1 and 7/1/2)]

3/2 Guaranteeing unknown (Majhul) and future debts

A valid guarantee may be given for debts, the exact amount of which is unknown. Similarly, a valid guarantee may be given for a debt that will arise in the future. However, it is permissible for the guarantor to withdraw such a guarantee before a future debt is actually created, after notifying the person having interest in the guarantee. This is called a “market (business) guarantee,” or a “guarantee of contractual obligation.” An example of this type is a third party’s guarantee to refund the price to the buyer if it appears that the sold commodity belongs to a person other than the seller and this guarantee is known as *Daman al-Dark* (dealers/business misrepresentation guarantee).

3/3 The effect of a personal guarantee

- 3/3/1 The creditor is entitled to claim the amount of his debt from either the debtor or the guarantor and he has the choice of claiming his right from either of them. However, the guarantor is entitled to arrange the order of liability, for example, by stipulating (at the conclusion of the contract of guarantee) that the creditor shall first claim payment from the principal debtor and that the creditor is entitled to recourse to the guarantor for payment only if the principal debtor refuses to fulfil his obligation.
- 3/3/2 If the creditor discharges the debtor from the debt, the guarantor is also discharged automatically from his liability. However, if the creditor discharges the guarantor from liability, the debtor remains in debt. If the guarantor secures a discount that results in paying an amount less than the original debt, the guarantor is entitled to recover only the amount he has actually paid to the creditor; he cannot demand that the debtor pay the debt in full ignoring the discount. This rule is intended to prevent a procedure being used that potentially leads to Riba. However, if the guarantor reaches an agreement with the creditor to settle the debt using as consideration a commodity of a different type from that in which the original debt was designated, the guarantor is entitled to recover the exact amount of the commodity provided as consideration for the debt, or the exact amount of the debt, whichever is less.
- 3/3/3 It is permissible for a personal guarantee contract to be designated in a separate contract. It can also be concluded together with, or before, or after, the conclusion of the contract of a credit transaction.
- 3/3/4 If an Institution manages transactions on the basis of Mudarabah or Musharakah or investment agency, it is not permitted for it to guarantee the fluctuations of currency exchange rates so that the investors will recover their investment shares irrespective of the behaviour of the currency market. Such a guarantee is prohibited

because it is tantamount to the Mudarib or partner or investment agent guaranteeing the capital of other partners or investors, which is prohibited by Shari'ah. [see items 2/21 and 2/2/2]

3/3/5 If the contract of a credit transaction stipulates that the debtor shall provide a guarantor and the debtor fails to provide one, the Institution is entitled to initiate legal action to force him to provide a guarantor or to terminate the contract.

4. Mortgage (Rahn)

It is to make a financial asset or so tied to a debt so that the asset or its value is used for repayment of the debt in case of default. [see Shari'ah Standard No. (39) on Mortgage]

5. Cases of Achieving the Objectives of Securities

5/1 Bringing forward future instalments in case of default on payment

It is permissible to include a term in a debt contract to the effect that, if the debtor defaults on the payment of one or more instalments, some or all of the future instalments shall fall due immediately, provided the default was not caused by unforeseeable intervening events or force majeure. However, this term shall not be effective until the debtor has been served with a reminder notice and after a reasonable period of time has elapsed.

5/2 Termination of a sale on deferred payment terms in case of failure to pay

The seller is entitled, in a contract of sale on a deferred payment basis, to stipulate that if the buyer fails to pay the price within a certain period of time, the seller is entitled to revoke the contract and repossess the sold asset without recourse to the courts.

6. Some Contemporary Applications of Securities

6/1 Letters of guarantee

6/1/1 It is not permissible to take remuneration for issuing a letter of guarantee, whether it is with cover or without cover, if the remuneration is intended as consideration for the guarantee

per se, since the amount guaranteed and the duration of the guarantee are usually taken into consideration in computing remuneration.

6/1/2 Asking an applicant for a letter of guarantee to bear administrative expenses incurred in issuing a letter of guarantee of either type (i.e. preliminary or final) is permissible in Shari'ah, provided the remuneration for such expenses do not exceed the commission that others would charge for such services. Where full or partial cover is provided, it is permissible, in estimating the expenses for issuing a letter of guarantee, to take into account anything that will reflect the actual service to be rendered in providing a cover for the transaction.

6/1/3 It is not permitted for the Institution to issue a letter of guarantee in favour of an applicant who will use it to acquire an interest-based loan or to conclude a prohibited transaction.

6/2 Documentary credit

It is a written undertaking by a bank (known as the issuer) given to the seller (the beneficiary) as per the buyer's (applicant's or orderer's) instruction or is issued by the bank for its own use, undertaking to pay up to a specified amount (in cash or through acceptance or discounting of a bill of exchange), within a certain period of time, provided that the seller present documents for the goods conforming to the instructions.

In brief, a documentary credit is an undertaking by a bank to pay subject to conformity of the documents to the contractual instructions. [see Shari'ah Standard No. (14) on Documentary Credit]

6/3 Use of cheques or promissory notes

There is no Shari'ah objection to obtaining cheques or promissory notes from the debtor (unless not allowed by law) as a means to force the debtor to make timely payment of instalments in cash, whereby if the debtor pays on time such cheques or promissory notes shall be returned to him, and in the event of default on payment they

may be produced for recovery. The party providing these cheques or promissory notes as security is entitled to obtain an undertaking from the Institution that they will be used only for timely recovery of its due debts without any addition.

6/4 Insurance for doubtful or bad debts

It is permissible to subscribe to an Islamic insurance coverage as security for debt obligations and it is not permissible that debts be insured on a conventional insurance basis.

6/5 Freezing cash deposits (blocking withdrawals)

6/5/1 In order to secure the future payment of debts on a single payment or an instalment basis, it is permissible for the Institution to stipulate, that it is entitled to freeze the customer's investment account, or to revoke his right to withdraw money from such an account entirely or to block an amount in the account equivalent to the debt, which is the preferred option. Nevertheless, the customer remains entitled to share profits on the whole balance of the investment account after deducting the Institution's share for acting as a Mudarib.

6/5/2 In a credit transaction, it is not permitted for the Institution to stipulate a right to freeze the customer's current account. However, a stipulation of this kind is allowed where the customer has freely, willingly and absolutely agreed to his current account to be frozen.

6/6 Third party guarantees (voluntary undertakings to compensate an investment loss)

It is permissible for a third party, other than the Mudarib or investment agent or one of the partners, to undertake voluntarily that he will compensate the investment losses of the party to whom the undertaking is given, provided this guarantee is not linked in any manner to the Mudarabah financing contract or investment agency contract.

6/7 Underwriting the subscription of shares issued (subscription guarantee)

6/7/1 It is permissible for the Institution to undertake that it will underwrite the remaining shares offered for subscription after the expiry of the offer period, provided the shares are underwritten at the offer value without any consideration for the underwriting per se.

6/7/2 The underwriter is entitled to receive consideration for a service it provides other than the guarantee, such as conducting a feasibility study or marketing the shares.

6/8 Guarantees in tenders, security deposits in Murabahah transactions and 'Arboun (Earnest Money)

6/8/1 It is permissible to obtain guarantees for tenders and this includes both the amounts paid for participating in the bid (primary cash security for participating in the bid) and the amounts paid when the contract is awarded to the successful bidder (final cash security providing evidence of ability to complete the project). Such amounts shall be considered as being held on trust by the offeror of the bid on behalf of the successful bidder, and are not viewed as 'Arboun (Earnest Money). Hence, such amounts are recoverable if they are intermingled with other amounts of money (i.e. irrespective of any unwanted circumstances). Moreover, it is not permissible to confiscate such amounts of money, except in compensation for an equivalent amount of financial damage actually sustained in the tendering process. Such amounts may be invested in the benefit of the customer with his consent, unless he requests it to be credited to his current account.

6/8/2 It is permissible for the Institution, in the case of a unilateral binding promise, to take a sum of money called *Hamish Jiddiyyah* (security deposit) from the purchase orderer (customer) as security for his promise. This sum of money is held on trust, not as

'Arboun, because no contract has been established. The rules set out in item 6/8/1 apply here. Where the customer fails to honour his binding promise, the Institution is not permitted to retain the security deposit as such. Instead, the Institution's rights are limited to deducting the amount of any damage actually incurred as a result of the breach, namely the difference between the cost of the item to the Institution and its selling price to a third party.

6/8/3 It is permissible to take 'Arboun from a buyer or lessee when a sale or lease contract is concluded, on condition that, if the contract is not terminated within the specified period during which the option to terminate the contract remains valid, such an amount will be considered as part of the consideration for the contract and, if the buyer or lessee fails to perform the contract within this period, the seller or lessor is entitled to retain the amount. It is, however, preferable that the Institution should refund to the customer any balance remaining after deducting from the 'Arboun the amount of any damage actually sustained by it.

6/9 Priority right of recovery and the right to follow up

6/9/1 The Institution is entitled to recover first its tangible items that were sold to or manufactured for a customer and have not been paid for and can be identified among the assets of the customer.

6/9/2 The Institution is entitled to protect the integrity of the subject of a guarantee, such as a mortgaged asset, and pursue a legal action against misusing it if it is established that the person holding it is using it in a manner that may lead to losses to be borne by the Institution.

6/9/3 The rights of the parties holding mortgages of security shall be given priority over the rights of the parties who are unsecured. [see Shari'ah Standard No. (39)]

6/9/4 In the event of bankruptcy or liquidation, the parties in charge of the liquidation have a preferential right or priority over other creditors in recovering their rights; i.e. the cost of any services provided in the process of liquidation. [see Shari'ah Standard No. (43) on Insolvency]

7. Date of Issuance of the Standard

This Standard was issued on 29 Safar 1422 A.H., corresponding to 23 May 2001 A.D.

Adoption of the Standard

The Shari'ah Standard on Guarantees was adopted by the Shari'ah Board in its meeting No. (6) held on 25-29 Safar 1422 A.H., corresponding to 19-23 May 2001 A.D.

Appendix (A)

Brief History of the Preparation of the Standard

In its meeting No. (2) held in Mecca on 10-14 Ramadan 1420 A.H., corresponding to 18-22 December 1999 A.D., the Shari'ah Board decided to give priority to the preparation of a Shari'ah Standard on Guarantees.

On Tuesday 27 Ramadan 1420 A.H., corresponding to 4 January 2000 A.D., a Shari'ah consultant was commissioned to prepare a juristic study and an exposure draft.

In its meeting held in Bahrain on 18-19 Rabi' I, 1421 A.H., corresponding to 20-21 June 2000 A.D., the Shari'ah Committee discussed the juristic study and made certain amendments to it. The committee also discussed the exposure draft of the Standard in its meeting No. (6) held in Bahrain on 20-21 Jumada II, 1421 A.H., corresponding to 18-19 September 2000 A.D., and asked the consultant to make some amendments in light of the comments made by the members.

In its meeting No. (7) held in Bahrain on 5-6 Sha'ban 1421 A.H., corresponding to 1-2 November 2000 A.D., the Shari'ah Committee discussed the exposure draft and made some relevant amendments.

The revised exposure draft of the standard was presented to the Shari'ah Board in its meeting No. (5) held in Mecca on 8-12 Ramadan 1421 A.H., corresponding to 4-8 December 2000 A.D. The Shari'ah Board made further amendments to the exposure draft of the standard and decided that it should be distributed to specialists and interested parties in order to obtain their comments in order to discuss them in a public hearing.

A public hearing was held in Bahrain on 4-5 Dhul-Hajjah 1421 A.H., corresponding to 27-28 February 2001 A.D. The public hearing was attended

by more than 30 participants representing central banks, Institutions, accounting firms, Shari'ah scholars, academics and others who are interested in this field. Members of the Shari'ah studies committee responded to the written comments that were sent prior to the public hearing as well as to the oral comments that were expressed in the public hearing.

The Shari'ah Committee held its meeting No. (8) on 16-17 Dhul-Hajjah 1421 A.H., corresponding to 11-12 March 2001 A.D., to discuss the comments made about the exposure draft. The committee made the necessary amendments in light of both the written comments that were received and oral comments that took place in the public hearing.

The Shari'ah Board in its meeting No. (6) held in Al-Madinah Al-Munawwarah on 25-29 Safar 1422 A.H., corresponding to 19-23 May 2001 A.D., discussed the amendments made by the Shari'ah Committee, and made necessary amendments. The Shari'ah Board unanimously adopted some of the items of the standard and some items were adopted by the majority vote of the members of the Shari'ah Board, as recorded in the minutes of the meetings of the Shari'ah Board.

The Shari'ah Standards Review Committee reviewed the standard in its meeting held in Muharram 1433 A.H., corresponding to November 2011 A.D., in the State of Qatar, and proposed after deliberation a set of amendments (additions, deletions, and rephrasing) as deemed necessary, and then submitted the proposed amendments to the Shari'ah Board for approval as it deemed necessary.

In its meeting No. (38) held in Al-Madinah Al-Munawwarah, Kingdom of Saudi Arabia on 28 Sha'ban - 1 Ramadan 1435 A.H., corresponding to 26-28 June 2014 A.D., the Shari'ah Board discussed the proposed amendments submitted by the Shari'ah Standards Review Committee. After deliberation, the Shari'ah Board approved necessary amendments, and the standard was adopted in its current amended version.

Appendix (B)

The Shari'ah Basis for the Standard

Permissibility of Guarantees and Its Relevance to Contracts

The basis of the permissibility of stipulating guarantees in contracts is that it protects property, which is one of the objectives of Shari'ah. The other authorities mentioned in the standard in support of each kind of guarantee can be cited as authority for the permissibility of guarantees in contracts.

Guarantees in Trust Contracts

Assets held on trust must be returned to their owners in the manner in which they were received and in their original physical state promptly after the owners demand their return. Allah, the Almighty, says: *{“Allah doth command you to render back your trusts to those to whom they are due”}*.⁽²⁾ Since such assets are not subject to exchange, they are purposely meant either for custody with permission to use them, such as assets on deposit, or for charitable acts, such as a loan of tangible assets. Therefore, the persons holding such assets are considered by the owners from the beginning as capable of returning them to their owners on demand, making them trustees, and as a principle of Shari'ah, a trustee is not held liable (for loss of, or damage to, an asset held on trust), except in circumstances of misconduct, negligence or violation of the conditions agreed upon, because in other circumstances it is inconsistent with the fundamental principle of trusts for a trustee to be held liable.

Written Documentation and Attestation

Written documentation is recommended by Shari'ah. This is the opinion of the majority of Fuqaha, in contrast to Ibn Hazm who argued that written documentation is an obligation (i.e. if one did not put his financial

(2) [Al-Nisa` (Women): 58].

transactions in writing he has committed a sin) relying on the literal meaning of the Qura'nic verse: ***{“O ye who believe! When you deal with each other, in transactions involving future obligations in a fixed period time, reduce them to writing”}***⁽³⁾ and the Quranic Verse: ***{“Disdain not to reduce to writing your contract for a future period, whether it be small or big”}***.⁽⁴⁾ The majority of Fuqaha have also inferred that this verse itself excluded written documentation in the cases of trustworthiness, as the last part of the following verse says: ***{“And if one of you deposits a thing on trust with another, let the trustee (faithfully) discharge his trust and left him fear Allah his Lord.”}***

It must be noted that customary practice is the basis in determining the form and evidential value of written documentation, because Shari'ah did not specify a particular manner of writing to be considered. As for the permissibility of attestation as documentation, the authority for that is the following Qura'nic verse: ***{“And get out two witnesses, out of your own men. And if there are not two men, then a man and two women, such as ye choose, for witnesses, so that if one of them errs, the other can remind her”}***.⁽⁵⁾

The evidential value of attestation according to traditional Fuqaha is stronger than that of written documentation. But in modern times, things have changed so that some laws rely on witnesses only in a very limited number of cases and paramount importance is given to written documentary evidence.

Personal Guarantees

Permissibility of personal guarantees

Personal guarantees derive their permissibility from the Qura'n, Sunnah, consensus and reasoning. In the Qura'n, Allah, the Almighty, says: ***{“They said: ‘We miss the great beaker of the king; for him who produces it, is (the reward of) a camel load; I will be bound by it’”}***.⁽⁶⁾ In Sunnah, there is the Hadith narrated by Salamah Ibn Al-Akwa', who said: “We were with the

(3) [Al Baqarah (The Cow): 282].

(4) [Al Baqarah (The Cow): 282].

(5) [Al Baqarah (The Cow): 282].

(6) [Yusuf (Joseph): 72].

Prophet (peace be upon him) when a deceased person was brought. They said, 'O Prophet of Allah, perform prayers on him.' He (peace be upon him) said, 'Has the deceased left anything?' They said, 'No.' He (peace be upon him) said, 'Is he in debt?' They said, 'Three dinars.' He said, 'Perform prayers on your companion.' Abu Qatadah said, 'O Messenger of Allah, perform prayer on him, and I am responsible for his debt.' Then the Prophet (peace be upon him) performed prayers on him."⁽⁷⁾ In another text of the Hadith, he (Qatadah) said: "I guarantee (to pay) his debt."⁽⁸⁾

The Fuqaha are unanimous on the permissibility of personal guarantees. Moreover, the need of people for personal guarantees to facilitate dealings with each other had also made them legitimate, particularly in the case of customers who lack a good credit record. In addition, personal guarantees encourage performance and prevent the contract from being breached and this security also justifies their permissibility.

The objection to taking consideration for personal guarantees is that giving a guarantee is one of the charitable acts that should be offered without consideration, and this ruling has generated consensus among the Fuqaha. Moreover, a personal guarantee indicates a readiness to give away the amount of a loan, which means that the guarantor will pay the loan (if the principal debtor fails to pay) and have recourse to the guaranteed person for fulfilment. Hence, it is not permissible to take consideration for a guarantee, because it is not permissible to take consideration for giving away the amount of the loan itself, since such consideration is considered to be Riba.

Guaranteeing unknown and future debts

The Shari'ah basis for the permissibility of guaranteeing the unknown is the general meaning of the Hadith: "*The guarantor is liable.*"⁽⁹⁾ because

(7) Related by Al-Bukhari in his "*Sahih*" [2: 800], Dar Ibn Kathir and Yamamah.

(8) "*Sunan Al-Nasa'i*" [7: 317]; "*Sunan Ibn Majah*", [2: 804]; and Al-Bayhaqi in "*Al-Sunan Al-Kubra*" [4: 95].

(9) The Hadith has been related by Ahmad, Abu Dawud, and Al-Tirmidhi: "*Al-Darari Al-Mudiyyah*" [1: 399], Dar Al-Jil; Ibn Majah in his "*Sunan Ibn Majah*" [2: 804], Dar Al-Fikr; and Al-Bayhaqi in "*Al-Sunan Al-Kubra*" [6: 72], Maktabat Dar Al-Baz.

this Hadith makes no distinction between guaranteeing the known and the unknown since there is no harm or element of dispute arising due to uncertainty here, because the unknown transaction guaranteed will become certain and known, and the guarantor will know, after the debt is incurred, the actual obligation he undertakes. Another authority for the permissibility of guaranteeing what is not known is the Quranic verse: *{“...for him who produces it, is (the reward of) a camel load and I will be bound by it”}*.⁽¹⁰⁾ Here, the guarantor guaranteed a camel load although it was not yet a debt.

The evidence for the creditor's right to demand payment from either the debtor or the guarantor is that the debt is established as liability of both of them, hence the right to demand payment from either of them. The permissibility for stipulating that the creditor has first to ask for payment from the principal debtor and that he may ask the guarantor for payment only if the debtor fails to pay, is based on an opinion in the Maliki school of law⁽¹¹⁾ and it is also an opinion of the Hanafis.⁽¹²⁾ These opinions argued that if the debtor is solvent then demanding payment from the guarantor is pointless, unless the debtor refuses to pay. So, the requirement that payment be first sought from the debtor has a Shari'ah basis as well as being a case of adherence to a principle of natural justice.

Bringing Forward Future Instalments in Case of Default in Payment

The basis for this condition is the Hadith of the Prophet (peace be upon him): *“Muslims are bound by the conditions they made,”*⁽¹³⁾ and because payment on a deferred basis is the right of the debtor, and the debtor may choose to pay before time and relinquish the deferral of the date of payment entirely. If this is the case, the date of payment may also be based on default so as to strengthen the collectibility of the debt and secure payment on time. The basis of the rule enabling the creditor to demand payment of all instalments in the event of default, instead of waiting until each instalment

(10) [Yusuf (Joseph): 72]. *“I will be bound by it”* means being a guarantor.

(11) Ibn Rushd, *“Al-Bayan Wa Al-Tahsil”* [11: 291].

(12) *“Bada`i` Al-Sana`i”* [7: 2423].

(13) Related by Al-Bayhaqi in *“Al-Sunan Al-Kubra”* [6: 79], Maktabat Dar Al-Baz; Al-Daraqutni in his *“Sunan Al-Daraqutni”* [10: 27], Dar Al-Ma`rifah; Ibn Abu Shaybah in his *“Musannaf”* [4: 450], Maktabat Al-Rushd; and Al-Tahawi in *“Sharh Ma`ani Al-Athar”* [4: 90], Dar Al-Kutub Al-`Ilmiyyah.

is due, is the possibility that during the period of delay in payment the debtor may find a means to conceal his assets and claim insolvency. The permissibility of this condition is confirmed by the Resolution No. (51) issued by the International Islamic Fiqh Academy.

Termination of a Sale on Deferred Payment Terms in Case of Failure to Pa

The basis for this is that the seller has consented to deferred payment only if it will not lead to a loss of what is due to him. This is the opinion of the majority of Fuqaha, as opposed to the Hanafis who have confined the creditor's right to litigation, unless he has stipulated the right to terminate the contract and "Muslims are bound by conditions they made."

Guarantees and Their Modern Applications

Letters of Guarantee

The basis of the rule that no remuneration may be taken for a guarantee per se is that it is a surety, and as such it is one of the contracts of charity since it involves a readiness to give away the amount of a loan for no consideration. The majority of Fuqaha agree that it is prohibited to take consideration for guarantee. However, issuing the letter of guarantee is a service that justifies charging fees.

The prohibition of issuing a letter of guarantee for unlawful acts is analogous to the prohibition of giving assistance in committing a sin. The Hadith: *"Allah curses the one who gives Riba and the one who takes it and the one who writes its contract and the two witnesses involved"*⁽¹⁴⁾ also supports this ruling, because the personal guarantor has a stronger role in establishing and recovering a debt than the writer of the contract and the witness mentioned in the Hadith.

Documentary credits

The basis for the permissibility of charging fees for a documentary credit is that issuing a documentary credit is a service performed in the interest of the applicant for the documentary credit, for which the Bank has the right to charge fees.

(14) Related by Muslim in his *"Sahih"* [3: 1219], Dar Ihya' Al-Turath Al-'Arabi; and the five compilers of Hadith, and see: Al-Shawkani *"Nayl Al-Awtar"* [5: 296], Dar Al-Jil.

Use of cheques or promissory notes

The Shari'ah basis for obtaining cheques or promissory notes from the debtor as a guarantee is the general sources on the permissibility of guarantees in general.

Insurance for debts

Islamic insurance is based on the principle of donation, and Gharar is tolerable in such conditions. In Islamic insurance, the instalments that are paid are provided within a framework of donations organised for the mutual benefit of the contributors to the insurance fund. The permissibility of Islamic insurance is confirmed by the resolutions issued by the Islamic Fiqh Academy of the World Muslim League⁽¹⁵⁾ and the International Islamic Fiqh Academy of the Organisation of Islamic Conference.⁽¹⁶⁾ Although this form of insurance falls within the meaning of a guarantee, the guarantee here is not provided in return for conditional consideration as such, hence the permissibility of subscribing to an Islamic insurance coverage as security for doubtful or bad debts.

Freezing cash deposits

The basis for the permissibility of stipulating a right to freeze a customer's investment account is the permissibility of pledging funds, in addition to the fact that the purpose behind such freezing is to be able to agree on a set-off if it appears that the pledgor of the balance is in debt to the bank. It is a form of mortgage to secure a possible future debt. The basis for the prohibition of stipulating a right to freeze a customer's current account is that such a right would be tantamount to a combination of a sale on deferred payment terms and a loan transaction; i.e., it amounts to a deferred sale with a condition to provide a loan, which is prohibited by Shari'ah.

Third party guarantees

The basis for third party guarantees is that they are a promise to volunteer to remedy a loss of capital under an investment contract with a party other

(15) The First Session, Resolution No. (5).

(16) Resolution No. 9 (9/2).

than the volunteer. This is a permissible act as a volunteer, as is evidenced in the Holy Qura'n: *{“No ground (of complaint) can there be against such as do right,”}*.⁽¹⁷⁾ A resolution passed by the International Islamic Fiqh Academy states as follows:

“There is no Shari'ah objection to mention in the prospectus of the issue or in the documents of Muqaradah (Mudarabah) bonds the promise of a third party, who is independent personally and in terms of financial liability from the two parties to the contract, to volunteer an amount of money for no consideration to be allocated to make good a loss on a particular project. However, this is circumscribed with a condition that such a promise should be an obligation independent from the Mudarabah contract. In other words, the third party's performance of his obligation should not be a condition for the enforcement of the contract and the conditions and liabilities of the parties to the contract. As such, holders of the bonds or the manager of the Mudarabah are not entitled to claim that they may fail to honour their obligations relating to their contracts because the volunteer failed to fulfil his promise because the performance of their obligations takes into consideration the promise to volunteer.”⁽¹⁸⁾

Underwriting the subscription of shares issued

If such underwriting is offered without consideration, it is considered as a personal guarantee for no consideration, and this is permissible in Shari'ah. However, if it is for consideration, the basis for its prohibition is what we have mentioned in respect to taking a commission for a guarantee. [see item 4/1]

Guarantees in tenders, security deposits in Murabahah transactions and 'Arboun (Earnest Money)

The basis for the permissibility of guarantees in tenders and earnest money is the afore-mentioned authority for guarantees in general. Both guarantees in tenders and security deposits are permissible because they facilitate obtaining compensation for actual damages in case of breach of contract. The basis for obtaining the earnest money to secure performance

(17) [Al-Tawbah (Repentance): 91].

(18) Resolution No. 30 (5/4)

is the practice of Umar Ibn Al-Khattab (may Allah be pleased with him) in the presence of some companions of the Prophet (peace be upon him), which has been permitted by Imam Ahmad. A resolution has been issued in connection with the permissibility of 'Arboun (Earnest Money) by the International Islamic Fiqh Academy.⁽¹⁹⁾

Priority right of recovery and the right to follow up

The basis for the permissibility of the priority of certain rights, such as those of liquidators, is that these rights are considerations that are determined by the judiciary on the basis of public interest. The basis for giving priority to a person whose assets per se have contributed to the increase of the bankrupt's assets, and have been located and identified, is the Hadith of the Prophet (peace be upon him): *"If one sells a commodity, and the owner thereof becomes bankrupt, and then he finds it without being altered, he has more right over it than the other creditors."*⁽²⁰⁾ A resolution in connection with the permissibility of preference was issued by the Second Fiqh Seminar hosted by Kuwait Finance House, based on a number of Fiqh rulings determining certain preferences that include priority in the recovery of debts. The right of following up the subject of a mortgage is based on the fact that the aim of the mortgage is to facilitate recovery of the amount of the debt and leaving the debtor without a right of follow-up will defeat this objective.

(19) Resolution No. 72 (3/8) in respect of 'Arboun (Earnest Money).

(20) Related by Al-Bukhari and Muslim with different texts as follows: *"If one finds his property without being altered in the possession of a bankrupt, he has more right over it than the other creditors"*: *"Sahih Al-Bukhari"* (H: 2402); and *"Sahih Muslim"* (H: 1559).

Appendix (C)

Definitions

Payables:

Debts that are absolutely payable and liabilities held on trust basis, either because of being contractually created, or because unjust enrichment has given rise to a liability for restitution.

Liabilities:

Liabilities held on trust basis, i.e., obligations that are not subject to compensation for any loss suffered except in circumstances of misconduct, negligence or violation of the conditions agreed upon.

