

Shari'ah Standard No. (51)

**Options to Revoke Contracts
Due to Incomplete Performance**



Contents

Subject	Page
Preface	1201
Statement of the Standard	1202
1. Scope of the Standard	1202
2. Option to Revoke Due to Defect	1202
3. Option to Revoke Owing to Deal Fragmentation	1204
4. Option to Revoke Due to Breach of Description	1205
5. Date of Issuance of the Standard	1206
Adoption of the Standard	1207
Appendices	
Appendix (a): Brief History of the Preparation of the Standard.....	1208
Appendix (b): The Shari'ah Basis for the Standard.....	1210



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

This Standard aims to explain the situations in which buyers have the option to revoke contracts due to reasons of defect, deal fragmentation and breach of description and how such options are exercised in the activities of 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 options to revoke contracts due to reasons of defect, deal fragmentation and breach of description. It does not cover options to revoke arising from breach of trust (dishonest inducement, deception and overcharging) or options of due diligence (cooling-off options, and options to revoke due to non-payment) as they have separate Shari'ah standards dedicated to them.

2. Option to Revoke Due to Defect

2/1 Definition

It is the option of a buyer to revoke or continue with the contract arising from a hidden defect that the buyer did not notice at the time of contract.

2/2 Conditions applicable to options to revoke due to defect

An option to revoke due to defect is subject to the following conditions:

2/2/1 Appearance of a material defect in the subject matter of the contract.

A material defect is a defect that renders the item defective according to custom, makes it unfit for purpose or diminishes its value.

2/2/2 The defective item being incapable of repair except by incurring cost.

2/2/3 The buyer being unaware of the hidden defect at the time of contract, irrespective of the seller's awareness of the defect at the time of the contract.

2/2/4 The contract not containing a clause excluding the seller's liability for defect (*Bay' al-Bara'ah*- sale on the basis of as is

where is). It is prohibited for the seller to exclude liability due to defect in Ijarah and Istisna'a contracts.

2/2/5 The hidden defect not being caused by the buyer.

2/3 Scope of the option to revoke due to defect

Options to revoke due to defect exist in commutative financial contracts such as sales, money exchange, division of wealth, settlement of debt by payment in kind and gift conditional upon receipt of consideration (*Hibat al-Thawab*).

2/4 Time limit

Defective items should be returned, after taking delivery of the object of sale and discovering the defect therein, within the period of time customarily allowed for revocation on such grounds.

2/5 Consequences of options to revoke due to defect

The buyer has the option either to revoke the contract and return the item or continue with the contract. If the buyer chooses to return the item after taking delivery, revocation is effected by mutual consent or court order. If the buyer has not taken delivery, and he has been aware of the defect before taking delivery, he can unilaterally revoke the contract by giving notice to the seller and is entitled upon revocation to a refund of the whole price by mutual consent or court order.

2/6 Conditions applicable to the return of sold items

Return of the item is subject to the following conditions:

2/6/1 Return of the item not resulting in the fragmentation of a package deal to which the seller does not consent. And the buyer shall be entitled to compensation against inferiority due to the defect (Arsh).

2/6/2 The item not being damaged or destroyed in the possession of the buyer, in which case the buyer is entitled only to compensation for the defect and is not entitled to return the item unless the seller accepts return of the damaged item.

2/6/3 There being nothing added to the item attached to it but did not grow out of it, which necessitates a price rebate, such as the erection of a building on land. Return of the item is not prevented, if the addition to the item is physically connected to it and grows out of it; or is physically separate from it whether it grows out of it, such as dividends on shares and rent from leased assets, or does not grow out of it.

2/6/4 In cases where return due to the defect is impossible (impractical), the buyer shall be entitled to compensation against inferiority caused by the defect.

2/7 Impediments preventing the return of sold items

The option to return the sold item is impeded by the non-fulfilment of any of the conditions provided in item 2/2.

2/8 Abating (of the option)

The option to revoke due to defect ceases (abates) in the following situations:

2/8/1 If the defect ceases before the buyer returns the item or payment of Arsh (compensation against inferiority due to the defect).

2/8/2 If the buyer expressly waives his option to revoke.

2/8/3 If the buyer expressly accepts the defective item.

2/8/4 If the buyer's conduct implicitly indicates that he has accepted the defective item, such as continuing to use the item, delaying return of the defective item longer than is customarily acceptable and without an excuse, exploiting or benefitting from the defective item or transferring ownership of the item after discovering the defect.

2/8/5 If the defective item is destroyed by the buyer.

3. Option to Revoke Owing to Deal Fragmentation

3/1 Definition

The option to revoke a contract owing to deal fragmentation is the option of the buyer to revoke a contract (a package deal) that no

longer includes everything that was contracted for, resulting in the package deal becoming fragmented.

3/2 Conditions applicable to the option to revoke owing to deal fragmentation

The option to revoke a contract owing to deal fragmentation is subject to the buyer not knowing that the deal would become fragmented.

3/3 Types of deal fragmentation in which the option to revoke is granted

3/3/1 When a person sells his own property along with the property of another person in one package without the consent of the other person or when a partner sells the partnership property in one package without the consent of the other partner.

3/3/2 When it transpires that part of the sold item(s) is the property of a third party.

3/3/3 When part of the sold item(s) is destroyed before delivery (actual or constructive).

3/3/4 When part of the sold item(s) in a Salam contract is not available on the delivery date. [see Shari'ah Standard No. (10) on Salam, item 5/8]

3/4 Prerequisites

Deal fragmentation entitles the buyer either to revoke the contract or accept what remains of the deal and pay the portion of the price corresponding to it. The buyer is not entitled to any compensation unless there is a defect in what remains of the sold item(s).

4. Option to Revoke Due to Breach of Description

4/1 Definition

The option to revoke due to breach of description is the option of a buyer to revoke the contract if the sold item does not meet a condition stipulated in the contract, explicitly or implicitly, such as a car having a specific color.

4/2 Requirements of valid descriptions

- 4/2/1 The description must be permissible by the Shari'ah.
- 4/2/2 The description must be specific and free from ambiguity (Gharar).
- 4/2/3 The description must relate to the purpose of the buyer or be the basis of an increase in price or of greater quality in the item, such as a requirement that a car be automatic.
- 4/2/4 The breach of description must occur at or before the time of delivery (actual or constructive) and must not be a subsequent occurrence.

4/3 Consequences of the option to revoke for breach of description

- 4/3/1 If the item fails to correspond to the minimum requirements of a description, the buyer is entitled to return the item or accept it for its full price without any entitlement to compensation.
- 4/3/2 If it is not possible to return the item, the buyer is entitled to a partial refund for the breach of description equal to the difference in price between an item that fulfills the description and one that does not.

4/4 Timing and cessation of options to revoke due to breach of description

The option to revoke for breach of description, like the option to revoke for defect, is granted immediately subject to custom and ceases in the circumstances in which the option to revoke due to defect ceases. [see item 2/7]

4/5 Transfer

The option to revoke for breach of description can transfer to all types of successors and assignees.

5. Date of Issuance of the Standard

The Shari'ah Board issued this standard on 21 Safar1434 A.H., corresponding to 4 January 2013 A.D.

Adoption of the Standard

The Shari'ah Board adopted the standard on Options to Revoke Contracts Due to Incomplete Performance in its meeting No. (34) held in the Kingdom of Bahrain on 20–21 Safar 1434 A.H., corresponding to 3–4 January 2013 A.D.

Appendix (A)

Brief History of the Preparation of the Standard

On 14 Rabi' II, 1429 A.H., corresponding to 20 April 2008 A.D., the Secretariat of AAOIFI decided to commission a Shari'ah consultant to prepare a juristic study on Options to Revoke Contracts Due to Incomplete Performance.

In its meeting held on 29 Jumada II, 1431 A.H., corresponding to 12 June 2010 A.D., the Shari'ah Standards Committee, discussed the study and approved it and assigned to the Shari'ah researcher the preparation of the exposure draft of the standard.

In its meeting held in Dubai (United Arab Emirates) on 24 Ramadan 1431 A.H., corresponding to 3 September 2010 A.D., the Shari'ah Standards Committee discussed the exposure draft of the standard and made some changes in the light of the comments and remarks of the members.

In its meeting No. (32) held in Al-Madinah Al-Munawwarah, on 8-9 Rabi' II, 1433 A.H., corresponding to 1-2 March 2012 A.D., the Shari'ah Board discussed the exposure draft of the standard and introduced the changes it deemed suitable.

The Secretariat of AAOIFI held a public hearing in the Kingdom of Bahrain on 16 Jumada II, 1433 A.H., corresponding to 7 May 2012 A.D. The public hearing was attended by representatives of central banks, institutions, auditing firms, Shari'ah scholars, academics and others interested in this field. The members of the Shari'ah Board and the Shari'ah Standards Committee responded to a number of observations and comments raised by the participants.

In its meeting No. (33) held in Makkah Al-Mukarramah on 19-21 Shawwal 1433 A.H., corresponding to 6-8 September 2012 A.D., the

Shari'ah Standard No. (51): Options to Revoke Contracts Due to Incomplete Performance

Shari'ah Board discussed the changes proposed at the public hearing and introduced the changes it deemed suitable to the draft exposure of the standard.

In its meeting No. (34) held in the Kingdom of Bahrain on 20-21 Safar 1434 A.H., corresponding to 3-4 November 2013 A.D., the Shari'ah Board discussed the exposure draft of the standard, introduced the changes that it deemed suitable and adopted the standard.

Appendix (B)

The Shari'ah Basis for the Standard

Option to Reconsider Due to Defect

- The basis for permissibility of the option to reconsider due to defect is the Hadith narrated by 'A'ishah (may Allah be pleased with her) that a man purchased a young serf, and then set him to work, then he found him to be "flawed" or "defective", so he returned him back (to the seller) on the grounds of the defect. Thereupon, the Prophet (peace be upon him) said: *"No yield without risk taking" and in another narration: "No gain without risk taking"*.⁽²⁾ Also, there is the Hadith on a sheep whose udder is tied up in order to look like a one full with milk. If the defect, lack of milk, is unveiled, then the buyer shall have the option either to keep it or to return it along with a Sa' of dates. All Schools of Fiqh (Madhahib) embraced this option, and that the key principle in the contracts of sale is freedom from defects.
- The basis for the stipulation of freedom from defects is what the companions (may Allah be pleased with them all) used to practice, and Othman (may Allah be pleased with him) issued a rule in favor of using this option in presence of the companions.⁽³⁾
- The basis for the effect of the option either to return the subject matter or keep the entire price –which is the standpoint of Hanafis and Shafis- is that the buyer has the right to return the subject-matter due to defect and the absence of intactness as generally dictated by the contract. The basis for non-entitlement to compensation (Arsh) in the case where the buyer keeps the subject-matter is that descriptions (features) are not considered to form part of the price in this case, and because the buyer did not consent that the sold item was transferred for a less than its stated price. The Han-

(2) Related by Abu Dawud and Al-Tirmidhi.

(3) Related by Malik in *"Al-Muwatta'"*; and Al-Bayhaqi in *"Al-Sunan Al-Kubra"* and he rendered it as an authenticate: *"Jami' Al-'Usul"* [2: 34].

balis were of the opinions that in case of return, the buyer shall have the right to request Arsh, corresponding to the inferiority caused by the defect.

Option of Deal Fragmentation

- The basis for permissibility of deal fragmentation is that it is a type of defect (some Fiqh references categorized it under the option to reconsider due to defect) and it becomes binding upon returning of a part of the object of sale.⁽⁴⁾
- The basis for the stipulation that the buyer shall not harbor prior knowledge about the deal coming into a point of defragmentation is that his knowledge is viewed as evidence to consent, and that the defect is not hidden or concealed.
- The basis for the effect of the option of defragmentation being either termination or holding into the remainder of his share in the price is that discounting an amount from the price for the whole deal in lieu of the missing part of the deal represents compensation, and no more than it, because the price (compensation) is for the two parts and is divided between them both.

Option of Breach of Description

- The permissibility of this option is the opinion of the majority of Fuqaha, while other Fuqaha categorized this option under option of deception (*Khiyar al-Tadlis*).
- The basis for the establishment of compensation due to incorrect description is that it is practically similar to the option of freedom from defect, in the case of objection to return the object of sale. And in the case where the buyer accepts to keep the object of sale, then he will possess it for the entire price -without application of Arsh- because what is missing here is a description, and descriptions do not have their corresponding part of the price in this instance.
- The basis for transferability of this option upon death to heirs, whether general or special, is that it falls in the category of physical asset ('Ayn) ownership.⁽⁵⁾



(4) "Al-Fatawa Al-Hindiyyah" [3: 83].

(5) "Fath Al-Qadir" [5: 1345]; and "Al-Bahr Al-Ra'iq" [6: 19].

