Interest under Shari′a

The issue of interest has been a religious and ethical dilemma for many Muslim businessmen since the early years of Islam for many reasons. First, usury, or riba, is very similar to some kinds of sales contracts, especially futures contracts for the sale of not-yet-existing subject matters, known as 'bay′ al salam'. The argument for riba in the Quran can be seen in the following verse: 'They said "Trade is like interest" while Allah has permitted trade and forbidden interest.'[39] Second, interest is the main motive for modern banking business and can be considered as the cornerstone of any modern economy.

Islam came to abolish some of the pre-Islamic practices in order to protect the whole society from their negative effects. In the pre-Islamic era, charging interest was a standard condition for any loan agreement; however, the total prohibition went through different stages and took a long time during the life of Prophet Muhammad to become final. When looking at the religious basis of the prohibition of riba, the complete ban has gone through four stages, starting with showing that riba is not recommended for Muslims and that they should avoid it as much as they can, and ending up with a definite prohibition.

The first stage discouraged people from charging interest over loans given to other people, a discouragement that can be understood through the following verse: 'That which you give as interest to increase within other people's wealth increases not with Allah; but that which you give in charity, seeking the goodwill of Allah, multiplies manifold.'[40]

In the second stage, the prohibition took the form of reminding Muslims what previous nations had done before the Quran showed that their practices were not the right thing to do. The following verse might indicate that Muslims should stop charging interest over loans: 'And for their taking interest even though it was forbidden for them, and their wrongful appropriation of other peoples' property, we have prepared for those among them who reject faith a grievous punishment.'[41]

The third stage clearly demonstrated that riba was prohibited and therefore a sin. It can be seen in the following verse that riba had not yet quite reached the level of being one of the major sins that Muslims must not even get close to: 'O believers, take not doubled and redoubled interest, and fear Allah so that you may prosper. Fear the fire which has been prepared for those who reject faith, and obey Allah and the Prophet so that you may receive mercy.'[42]

In the fourth and final stages, the prohibition of riba became final – since then it has been considered as one of the major sins, i.e., very close to murder, worse than adultery and similar in guilt to terrorism, which can be understood through the following verses of the Quran:

39 The Quran 1: 275.
40 The Quran 30: 39.
41 The Quran 4: 161.
42 The Quran 2: 130.

> O believers, fear Allah, and give up the interest that remains outstanding if you are believers;[43]

> Those who charge interest shall be raised like those who have been driven to madness by the touch of the Devil; this is because they say: "Trade is like interest" while Allah has permitted trade and forbidden interest. Hence those who have received the admonition from their Lord and gave up may have what has already passed, their case being entrusted to Allah; but those who revert shall be the inhabitants of the fire and abide therein for ever.[44]

This latter Quranic verse determines the legal basis for settling disputes involving interest or riba. Judges in Shari′a courts and *Diwan Almazalim* apply the principle established by this verse when deciding on any disputes or when reviewing arbitral awards: 'If you do not do so, then be sure of being at war with Allah and His Messenger. But, if you repent, you can have your principal. Neither should you commit injustice nor should you be subjected to it.'[45] In accordance with the teachings of this verse, interest must be avoided; however, if a person is involved in a usurious transaction he must not take more than the principal amount that he lent and interest must be excluded from any Shari′a-compliant judgment. The prohibition of riba in the Sunna was not just a restricted prohibition like the prohibition of many unlawful actions. The prohibition of interest followed the doctrine of extended prohibition, i.e., the prohibition covers all activities related to the prohibited subject matter and all the people involved in it are sinners on an equal basis.

The doctrine of extended prohibition of interest was established by the following Hadeeth: 'Prophet Muhammad cursed the receiver and the payer of riba, the one who records it and the witnesses to the transaction and said: they are all alike [in the sin].'[46] This Hadeeth can also be the legal basis for arguing for the prohibition of the functions of the Committee for the Settlement of Banking Disputes, as when the Committee upholds a riba transaction, it is considered to be involved in it, if not as the one who records it then as witness to the transaction. Moreover, another Hadeeth establishing a general rule for detecting unlawful transactions reads as follows: '[A]ny loan attract[ing] a benefit is riba.'[47] This rule is a very important safety measure against certain practices employed by some 'Islamic banks', which take advantage of differences in legal opinion among scholars with regard to the scope of the prohibition of riba. Riba is generally classified as unlawful

43 The Quran 1: 278.

44 The Quran 1: 275.

45 The Quran 1: 279.

46 Al-Imam Alzaylai′e, *Tabeen Alhaqaiq Sharh Kanz Aldaqaiq* (1st edn., Dar Alkotoub Alilmiyah, 2000), Vol. 4, p. 84.

47 Supra n. 30, Vogel, p. 77.

advantage by way of excess, as in '*riba alfadl*', and rescheduling of debt, as in '*riba alnasi'ah*'.[48]

The issue of riba alfadl arises in contracts of sale where there is an increase in the terms of exchange and the subject matter of the contract and consideration are identical. For instance, the exchange of a certain amount of US dollars for a higher amount of US dollars can be considered as riba, but if the consideration is different from the subject matter, as in the case of exchanging US dollars for Saudi riyals, there is no riba as long as the exchange is made on the spot.[49] There are some similarities between this class of riba and the practices of some Islamic banks nowadays, as some of them avoid riba alnasi′ah to get involved in riba alfadl. The law on riba alfadl was established by the following Hadeeth:

> [T]he selling of gold for gold is riba (usury) except if the exchange is from hand to hand and equal in amount and similarly, the selling of silver for silver is riba (usury) unless it is from hand to hand and equal in amount.[50]

Riba alnasi′ah, mostly referred to as riba aljahiliyah or, sometimes, the obvious riba, literally means 'the riba of the pre-Islamic era', because it was a very common practice among Arabs before Islam. This type of riba is similar to charging interest over loans and to delaying damages. It has been reported that Prophet Muhammad described all pre-Islam riba contracts as and cancelled his own uncle's Moreover, in the treaty of the Prophet with the Christians of Najran,[51] the Prophet cancelled the interest accrued on their debts, which had originated in the pre-Islamic period.[52]

For the sake of representing some of their practices as Shari′a compliant, some of the pioneers of modern Islamic banking have adopted the narrowest sense available for determining riba. They recognize the latter type only, i.e., riba alnasi′ah, arguing that it is the only prohibited practice mentioned in the Quran. They also rely on the reasoning of some of the companions of Prophet Muhammad, who said: '[T]here is no riba except riba alnasi′ah.'[53]

Having said that interest is prohibited under Shari′a, we should explore the reason behind this prohibition. There are many social, ethical and economic factors supporting the prohibition of riba, which have been summarized by Kula as follows:

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48 H. Ramadan, *Understanding Islamic Law from Classical to Contemporary* (1st edn., Alta Mira Press, 2006), p. 117.

49 Ibid.

50 Supra n. 28, El-Gamal, p. 68.

51 Najran is a city in the south of Saudi Arabia.

52 A. Saeed, *Islamic Banking and Interest: A Study of the Prohibition of Riba and its Contemporary Interpretation* (2nd edn., Brill Publisher, 1999), p. 30.

53 Ibid.

> The reason why usury is prohibited in Islam is manifold. First, the taking of interest, in the main, implies appropriating another person's property without giving him/her anything in exchange, because one who lends one pound for two pounds gets an extra pound for "no real effort". Second, dependence on interest prevents some people from working for a living, since the person with money can earn much more through interest without working for it. In this way individuals with money who will not bother to take the trouble of running a business will inevitably undermine the worth of work in the community. This will not only deprive the individuals with wealth of justly earned benefits, but it will also depreciate the wellbeing of the Islamic community for it is not possible to sustain the flow of goods and services by simply borrowing and lending money alone. The third and perhaps the most important aspect of riba is that it is, essentially, a transfer of money from the "poor" to the "rich", which is contrary to Islamic teaching.[54]

The financial crisis of 2008/09 showed a collapse in the value of banking assets which the Quran uses different terms to describe such as shrink and crunch.[55] The prohibition of riba can be considered as one of the main principles in Islamic economics nowadays. Modern economists have defined riba in the new contexts as any unjustifiable increase in capital, whether through loans or sales. More precisely, any positive, fixed, predetermined rate tied to the maturity and amount of the principal (i.e., guaranteed regardless of the performance of the investment).[56] The distinction should be made between riba and the rate of return or profit on capital, as Islam encourages the earning and sharing of profits, because profits represent a successful entrepreneurship and the creation of additional wealth. Interest, however, is considered as a cost that is accrued regardless of the outcome of the business operations and that may not create wealth if there are business losses.[57]

To sum up, all forms of interest charged over loans are totally prohibited under Shari′a and contradict the public policy of Saudi Arabia. A contract involving such terms is null and void in the part including the prohibited action. This view has been upheld by the teachings of all fiqh schools, the fatawa of the Ulama, and the judgments of Shari′a courts and the Board of Grievances. For instance, the Minister of Justice ordered all Shari′a courts and kitabat aladl, or 'notaries', not to authenticate the mortgages of commercial bank loans on which such banks take interest from the debtor by a certain percentage. The order covers any agreement or contract involving the payment of interest because it is prohibited by Shari′a.[58]

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54 E. Kula, 'Is Contemporary Interest Rate in Conflict with Islamic Ethics?', *Kyklos International Review for Social Sciences*, 61/1 (2008), pp. 45–49.

55 The Quran 1: 276.

56 Z. Iqbal and H. Tsubota, *Emerging Islamic Capital Markets: A Quickening Pace and New Potential* (World Bank Publications, 2006), p. 6.

57 Ibid.

58 See the Minister of Justice Circular No. 107/2/T dated 25/08/1389 H. (1969).

The Minister of Justice's order was upheld by the Supreme Judicial Council, which prohibited borrowing from commercial banks because they charge interest. The same decision exempts judges from deciding on disputes that involve the payment of any form of interest or loans associated with benefits.[59] It can be said that when kitabat aladl refuse to authenticate loan agreements, they might go against the injunction provided in one of the verses of the Quran that obliges them to authenticate any agreement, as they are not held responsible for their content. That verse reads as follows:

> O you who believe! When you contract a debt for a fixed term, record it in writing. Let a scribe record it in writing between you in (terms of) equity. No scribe should refuse to write as Allah hath taught him, so let him write, and let him who incurred the debt dictate, and let him observe his duty to Allah his Lord, and diminish naught thereof.[60]

Interest is prohibited under Shari′a as applied in Saudi Arabia, but the overall status is not really clear and a great deal of ambiguity surrounds the issue as a whole. This might be owing to the fact that the two bodies of law, i.e., Shari′a and the statute, are applied in parallel with the theoretical supremacy of Shari′a ruling. Current practice in Saudi Arabia has not identified whether riba is prohibited; however, it can be observed that even if riba is prohibited the prohibition is unenforceable in the sense that a person or a bank can charge interest as long as no dispute reaches the authority.

Arbitral awards entitling one of the parties to perform any unacceptable act under Shari′a, such as paying interest, will be set aside and the Board of Grievances will not enforce the parts contradicting Shari′a. A typical case in which a party seeks the enforcement of an arbitral award including interest can be seen in the following. An application for the enforcement of an arbitral award made in Bahrain was refused because it entitled one of the parties to pay interest. The Board allowed the enforcement of the part that complied with Shari′a only and the losing party was forced to repay the principal but without interest.[61]

Although banks claiming interest is against Shari′a, a client refusing the performance of a binding contract is against Shari′a as well, because it contradicts one of the main principles of Shari′a contract law, which is Alaqd Shari′ at Almouta′qedeen, Arabic for *Pacta Sunt Servanda*. The non-performance of a contract may contradict some of the Quranic texts such as: 'O ye who believe! Fulfil (all) obligations.'[62] Nonetheless, these principles can be easily challenged by

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59 See the decision of the Supreme Judicial Council No. 291 dated 25/10/1401 H. (1980).

60 The Quran 1: 282.

61 *Diwan Almazalim* decision No. 19/28 of 1399 H. (1979).

62 The Quran 5: 1.

the assumption that Shari′a prevails over the terms of any contract if the contract provides for a breach of one of the established principles of Shari′a.[63]

Interest under the Banking Regulations

The banking system is the heart of any modern economy and a strong economy cannot exist without a sound banking system.[64] From this fact, Saudi Arabia had to allow the establishment of commercial banks and the first Saudi bank was established in the 1930s. Banks started, from that time, to provide services and charge interest – the banking network soon expanded, especially in the 1960s and 1970s. The oil boom of the 1970s resulted in the establishment of some public funds that started lending to individuals and certain kinds of business with zero interest and on very flexible terms.[65] The oil boom also resulted in an accumulation of a huge amount of cash and liquid assets in a very short period of time, which led commercial banks to be more generous in providing their facilities without thorough consideration of the creditworthiness of their clients. Following that, banks started to suffer from a major legal problem represented in the refusal of Shari′a courts and the Committee for the Settlement of Commercial Disputes to recognize the validity of interest in banking transactions. The official position was not clear as the Government allowed Saudi banks to charge interest as long as it was necessary for the financial system and served the public interest, but it refused to recognize it in the case of disputes.

Despite article 149 of the Code of Commercial Courts of 1931, there is no mention of interest in Saudi regulations.[66] Financial regulations in Saudi Arabia do not give a clear answer to the question of whether charging interest on loans or awarding interest in arbitral awards is a permitted action. Even the Banking Control Act and its implementing rules did not mention the word interest, or fawaied, in its text. The situation is truly vague and confusing to the extent that nobody is able to determine whether interest is legal or illegal. There are different reasons for this, such as that riba was practised for many decades even though such practices contradict the main principles of Shari′a and that the Government

63 Supra n. 46, Al Imam Alzaylai′e, Vol. 4, p. 98.

64 R. Sylla, 'Financial Systems and Economic Modernization', *Journal of Economic History*, 62 (2002), pp. 277–92.

65 These funds were established by the Government, and they work under its direct supervision: The Saudi Arabian Agricultural Fund established in 1963; The Saudi Credit Bank founded in 1971; The Public Investment Fund created in 1973; The Saudi Industrial Development Fund established in 1974; The Real Estate Development Fund established in 1974.

66 Article 149 of the Code of Commercial Court does not really deal with interest charged over loans; it deals with one of the tricks applied by the Islamic bank to circumvent the prohibited riba. The example given in that article describes exactly the Tawarrouq transactions applied by Islamic banks nowadays.

itself deals with it in some of its contracts. Having said that riba violates Shari′a, there is no punishment for riba dealing – all that the judicial bodies do is annul the contradicting part of the contract.

It is appropriate to quote a conversation between King Faisal ben Abdul-Aziz (1903–1975) and a businessman, which shows that some regulatory bodies were more or less impartial with regard to banking interest. A bank customer complained to King Faisal that his bank was claiming interest, which he refused to pay because it is against Shari′a. The businessman expected the King to abolish the payment of interest but the King said that, since the bank granted the complainant a certain facility for a specified period, and he refused to pay interest, the complainant must return this favour to the bank and give the bank an equal amount for an identical period, after which time the bank is to repay it to him without interest. The complainant is said to have settled the interest to his bank without further objection.[67] By the early 1980s, banks complained to the authorities, arguing that they were losing too much and that the risk was too high. This complaint led to the establishment of the Committee for the Settlement of Banking Disputes in 1987.[68] The establishment of the Committee as a last resort for banks did not serve the banks' objectives in full and interest remained an avoidable obligation.

As a general rule, Saudi law is applicable to all governmental contracts. This choice of law may indicate that whatever the Government stipulates is not against the law or public policy. The practice of the Saudi Government adds more ambiguity, however, as charging interest became a valid practice in most of the former governmental contracts, both domestically and internationally. For instance, the recent gas concession agreements concluded in 2004 have a specific clause for interest charged on the amount of the financial guarantee in case of late payment. Article 18 in all three gas concession agreements provides for interest to be charged for late payment at the rate of LIBOR plus 1 per cent, which is exactly the prohibited riba under Shari′a.[69] Moreover, and contrary to its Charter, the Saudi Arabian Monetary Agency, 'SAMA', receives interest on assets deposited or invested with international financial institutions.[70] For one reason or another, the Saudi Government has been investing in US Treasury securities, which are simply debt certificates with interest charged over them.[71] In addition, the Government of Saudi Arabia has been financing its budget deficit through internal borrowing where the major lenders are the General Organization for Social Insurance and the Pension and Retirement Fund. Both organizations work under the supervision of

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67 M. Alameldin, 'Banking Disputes in Saudi Arabia', *International Financial Law Review*, 10 (1991), pp. 36–38.

68 Ibid.

69 See article 18 of the concession agreement between Saudi Arabia and Lukoil Saudi Arabia Ltd. *Umm Alqura Gazette*, issue No. 3990 dated 15/03/1425 H. (04/05/2005).

70 *Saudi Arabian Monetary Agency v. Dresnder Bank AG* (2003), WL 23145143.

71 See, generally, D. Spiro, *The Hidden Hand of American Hegemony: Petrodollar Recycling and International Markets* (1st edn., Cornell University Publication, 1999).

the Ministry of Finance and the Government has been serving the debt owed to those funds since the mid-1980s with a total interest accounting for SR 30 billion in the year 2000.[72] It can be said that charging interest is a governmental practice, but it does not usually apply to domestic transactions, i.e., contracts within the private sector other than banks, for the reason that *Diwan Almazalim* is the applicable forum for settling disputes arising out of the execution of such contracts and the *Diwan* does not recognize interest. It can be said again that interest payment is prohibited under Saudi law, but the prohibition is unenforceable as long as the parties voluntarily comply with their agreement.

The clash on this very specific legal issue represents a bigger point of controversy between two schools of thought within the Saudi authorities, and even within the society as a whole. A conservative party who rejects any attempt at reform or development and insists on leaving this vague situation against a larger group who seeks the modernization of the system without prejudice to the established principles and moral values of the society and arbitration in such an economically, religiously sensitive issue is one example of this clash.[73]

The Settlement of Banking Disputes in Saudi Arabia

Having said that interest is partly contrary to the public policy of Saudi Arabia and that arbitral awards should not include interest to render them enforceable, this section will examine the ways of settling such disputes in Saudi Arabia. First of all, Shari′a courts and *Diwan Almazalim* are not competent for the settlement of disputes relating to banking activities.[74] In addition, if a claim for interest is brought before Shari′a courts or *Diwan Almazalim*, the contract will be considered null and void in the part that violates Shari′a law. Therefore, the available remedies refer the dispute to arbitration, the Committee for the Settlement of Banking Disputes, or the Committee for the Settlement of Negotiable Instruments Disputes.

Arbitration

The previous chapter examined arbitration law and practice in the case of normal commercial dealings that do not violate the principles of Shari′a or public policy. The following part of this chapter will examine arbitration in disputes related to

72 A. Shoult, *Doing Business with Saudi Arabia* (3rd edn., GMB Publishing Ltd, 2006), p. 42.

73 The Chairman *of Diwan Almazalim*, Sheik Muhammad Alissa. *Okaz Newspaper*, issue No. 2459 dated 11/03/2008. The Sheik added that some judges even oppose computerizing the archive system in addition to the reform of some existing regulations and procedures.

74 Royal Order No. 729/8 dated 10/07/1407 H. (1987).

domestic conventional banking in Saudi Arabia. As concluded above, arbitral awards violating Shari′a law are of no effect and cannot be enforced in Saudi Arabia, either wholly or at least in the contradicting part of the award. Even though arbitration is an independent dispute resolution method, arbitration is found to be attached to the domestic legal system and the public order of the place of the issuance and enforcement, for the reason that arbitral awards cannot be enforced unless they are judicially approved in the place of enforcement. They should be, at the same time, valid at the place of issuance. It can be said that, unlike other neighbouring states, there is no way whatsoever to enforce an arbitral award concerning domestic conventional banking in Saudi Arabia if it provides for the performance of a prohibited act under Shari′a. Prior to the establishment of the Committee for the Settlement of Banking Disputes, arbitration was the only available remedy for banks; nonetheless, the enforcement of the award was totally dependent on the good faith of the parties to the dispute. For instance, in a loan agreement concluded in 1985, a Saudi bank agreed to settle a dispute that arose between it and a Saudi businessman, who refused to serve his debt by means of arbitration in Saudi Arabia subject to the ICC arbitration rules and under the supervision of the Jeddah Chamber of Commerce and Industry. The final award upheld the bank's right to receive interest on the principal amount in addition to the immediate repayment of the principal amount in cash. The arbitration panel applied the principle of Alaqd Shari′ at Almouta′qedeen, where the terms of the contract prevail over the law and arbitrators should rely on it when issuing their decisions without prejudice to the public order. When the bank filed a request for the enforcement of the award, the *Diwan* rejected the enforcement of the part contradicting Shari′a and gave the bank a choice between executing the award in the part compliant with Shari′a or referring the whole dispute to the competent authority of that time, i.e., the Committee for the Settlement of Commercial Disputes, to decide it anew. In another case, the *Diwan* blocked all possible solutions, rejected the whole award on the grounds of the prohibition of the subject matter of the dispute and denied jurisdiction on the case. The bank had to settle the dispute through conciliation with the debtor, who had the upper hand at that time and asked for rescheduling of the principal only, which the bank had to agree upon as the very last resort. In a number of arbitration cases concluded before the establishment of the Committee for the Settlement of Banking Disputes the *Diwan* gave the party seeking the enforcement of the arbitral award a choice between executing the Shari′a-compliant part of the award or referring the case to the Committee for the Settlement of Commercial Disputes under the Ministry of Commerce and Industry. However, on most occasions the *Diwan* rejects the enforcement of an arbitral award, leaving no room for alternative remedies. In such cases, the parties to the dispute have to initiate a new claim before the competent authority, which is very costly and time-consuming.

After the establishment of the Committee for the Settlement of Banking Disputes, arbitration became less attractive to banks as a method for settling domestic disputes, as resorting to the Committee for the Settlement of Banking

Disputes under SAMA gives banks a better chance of recovering the outstanding claims for interest. Moreover, in some circumstances, arbitration is a useless dispute settlement mechanism for banks owing to the *Diwan*'s inflexibility or even hostility against banks, as the *Diwan* considers all banking activities to be violations of Shari′a. The legal doctrine of 'ma boniya ala batil fahowa batil' applied by the *Diwan* provides for the illegality of all actions and practices if they are based on illegal principles, which might be one of the legal basis for denying the enforcement of arbitral awards providing for interest.[75] It can be assumed that the *Diwan* regards arbitration agreements and awards as illegal because of the nature of the underlying contract, which is a void contract under Shari′a.

As a result, the number of arbitration cases in which banks are involved has become very limited and, practically, banks in Saudi Arabia do not resort to arbitration any more in disputes relating to domestic conventional banking. The banks refrain from resorting to arbitration in domestic conventional contracts because the Committee for the Settlement of Banking Disputes of SAMA gives better solutions, as it looks at the dispute from a contractual point of view without the strict adherence to Shari′a rules applied by the *Diwan*. Therefore, arbitration remains a very speculative business while disputing parties and their lawyers navigate through legal uncertainty.

It has been noticed that the *Diwan* denies jurisdiction over any claim involving banks, even if the case falls within the *Diwan*'s general jurisdiction as the competent authority for the enforcement of arbitral awards in the kingdom. In the following case, the *Diwan* rejected the whole application for the enforcement of a domestic award on the grounds of having banks as parties to the dispute. The application for the enforcement of an arbitral award in relation to a dispute involving a Saudi company and two national banks was filed but rejected by the *Diwan* on the grounds of lacking jurisdiction to hear disputes in which a bank is involved.[76] In its decision, the *Diwan* quoted Royal Order No. 8/729 of 1407 H. (1987) as the basis for its refusal; however, the previous royal order determines the competent authority for the settlement of a banking dispute. The *Diwan*, when reviewing the arbitral award, is not settling the dispute; it is merely enforcing the decision of the arbitration committee with regard to the dispute after a general review of the award. It was a disappointment when the *Diwan* exceeded its terms of reference and tried to decide on the case anew. Accordingly, the presence of a bank as a party to the dispute can be grounds for setting aside an arbitral award without looking at the merit of the award itself, which can be considered as discrimination against banks. On the other hand, it can be said that there was a misunderstanding by the *Diwan* because the *Diwan* treated the enforcement application in a manner similar to treating an initial claim where, if it were the case, the reasoning of the *Diwan*

75 See *Diwan Almazalim* decision No. 11/D/F/2 of 1417 H. (1997). The legal doctrine of 'ma boniya ala batil fahowa batil' can be translated as 'anything based on something illegal is illegal'.

76 *Diwan Almazalim* decision No. 50/1418 dated 24/01/1409 H. (1988).

would be accurate. However, as the application was for the enforcement of a final arbitral award, the *Diwan* should not have intervened in such a discriminatory way. In a case where the party seeking the enforcement of the arbitral award insisted on the full enforcement of the award, the *Diwan* gave the option of referring the whole case to the competent authority, i.e., the Committee for the Settlement of Banking Disputes, which was supposed to be the second option after looking at the award. The *Diwan* declined to look at the award in the first stage on the grounds of having banks as parties to the arbitration. In another case, after the parties to the dispute spent a great deal of time and money, the award was set aside by the *Diwan* even though none of the parties challenged it. This last case shows the main difference between arbitration under the *Diwan* and the judgments of the Committee for the Settlement of Banking Disputes, which are binding on the parties if they are not opposed by the parties before issuing the award, as will be seen below.

It can be assumed that the *Diwan* follows one of the opinions under the Hanbali school, which considers contracts related to prohibited subject matters as null and void – there is therefore no real dispute because the whole transaction is of no value at all.[77] Nonetheless, the *Diwan*'s practices led to a movement among banks to avoid the jurisdiction of the Saudi authorities over their transactions, as will be discussed below. Yet, the high level of legal risk also encouraged banks to move toward Islamic banking, which seems to be ethically acceptable for customers and judges and has proved to be more profitable and less risky for banks in Saudi Arabia.

In international banking transactions where at least one of the parties to the dispute is considered to be a foreign party, even though it is not, parties to the contract can stipulate to arbitrate anywhere outside Saudi Arabia, which is usually their first preference. In any scenario, Shari′a secures its position by not allowing the enforcement of arbitral awards contradicting it, as the enforcement order must be filtered by the *Diwan* in the light of Shari′a ruling. However, arbitration is not the favourite dispute settlement mechanism, as in most cases the parties to the contract stipulate that English law or the law of New York is the proper law of the contract and therefore that London or New York is the appropriate forum. This tactic is mainly preferred by banks because there are no impediments to the enforcement of interest and other prohibited or disputed sale contracts like in Saudi Arabia. By doing so, the Saudi court will not be involved in the dispute by any means; however, if the arbitration award is brought to Saudi Arabia for the sake of enforcement, it will be regarded as invalid and the *Diwan* will consider it a circumvention to avoid the jurisdiction of the Saudi judiciary. In most cases, the parties to the dispute are wholly Saudis but the legal entity is incorporated somewhere outside Saudi Arabia, so they would be considered as foreign parties, as in the following example. The case of *Islamic Investment Company of the Gulf (Bahamas) Ltd v Symphony Gems NV and others* is a clear example of such tactics of circumvention to avoid the application of Shari′a law on transactions where the

77 Supra n. 46, Alzaylai′e, Vol. 4, p. 101.