

*This Article was published in The Lebanese Review of Arbitration, No. 16, 2000.*

### **ARBITRABILITY IN ISLAMIC LAW**

Rights in Islam are divided into three categories: rights of Allah, people's rights, and rights composed of both rights. The question here is which rights could be subject to arbitration and considered being arbitrable?

Scholars have agreed that matters subject to arbitration must be arbitrable. They agreed that any thing that cannot be subject of conciliation could neither be arbitrable. This principle is embodied in the provisions of different Arab and Islamic states, since Islamic law still determining the question of arbitrability in most of these states as in Saudi Arabia for example.

According to the "*Medjella* of Legal Provisions" which is considered to be the first codification of the *Shari'a* (Islamic Law) under the Ottoman Empire, it is admitted that arbitration is:

- (1) Compulsory in disputes leading to a separation of husband and wife.
- (2) Authorised with respect to disputes on goods or property.<sup>1</sup>

The *Medjella* covers only civil law matters, and the origins of most civil codes in the different Islamic countries are derived from it, even though it contains a whole section dedicated to arbitration, this section entitled 'Book of the Judicial Organisation and of Procedure'.<sup>2</sup>

The *Qur'an*, the main source of *Shari'a*, excludes certain subjects from the scope of arbitration, such as guardianship over orphans, which must obligatory be referred to courts of law.

As a general rule, arbitration is not authorised in those matters relating to the 'Rights of Allah' or to public order, the field of which is quite large, covering criminal law as well as those patrimonial rights for which a resort to arbitration would be equivalent to an authorised compromise.<sup>3</sup>

Generally speaking, the jurisdiction of arbitrators has a lesser scope than that of judge and covers only matters subject to compromise and conciliation.

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<sup>1</sup> Article 1841 of the *Medjella*.

<sup>2</sup> Section 4 of Book 16 (Articles 1841 to 1851).

<sup>3</sup> El-Ahdab, A., *Arbitration with the Arab Countries*, Kluwer, 1990, p. 39.

Rules on arbitrability in Islamic law can be summarised as follows:

- 1- Products deemed *haram* are not arbitrable, e.g. pork, alcohol, (*res nullius*).
- 2- Rights falling within the jurisdiction of religious courts are not arbitrable, which include *hadd*, and the penalties fixed by the Prophet which are irremissible; for example, theft, adultery, consumption of alcoholic drinks and apostasy. It is always possible to arbitrate on the financial consequences of offences other than *hadd*.
- 3- The arbitrability of matters relating to personal status such as marriage, affiliation, divorce and the guardianship of minors is subject to controversy between the schools of Islamic jurisprudence.<sup>4</sup>

*Shari'a* expressly prohibits the taking of interest, or *riba*;<sup>5</sup> the rationale for prohibiting the payment of interest could be summarised as follows:

- 1- Interest or usury reinforces the tendency for wealth to accumulate in the hands of a few, and thereby diminishes man's concern for his fellow man.
- 2- Islam does not allow gain from financial activity unless the beneficiary is also subject to the risk of potential loss; the legal guarantee of at least nominal interest would be viewed as guaranteed gain.
- 3- Islam regards the accumulation of wealth through interest as selfish compared with accumulation through hard work and personal activity.<sup>6</sup>

A practical example showing that interest is non-arbitrable in Islamic law is the ICC arbitration, which has taken place in the former North Yemen Republic. The dispute has arisen between a Yemeni governmental agency and West German company over implementing an agreement for providing services and management of breeding project, the sole arbitrator in this case has refused to grant the German party interest because it contradicts with Article 352 of the Yemeni Civil Code which considers any agreement of

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<sup>4</sup> Saleh, S., "The Recognition and Enforcement of Foreign Arbitral Awards in the States of the Arab Middle East," in Lew, J. (ed.), *Contemporary Problems in International Arbitration* (1989) at 350.

<sup>5</sup> The definition of the word *riba* has been the subject of a protracted jurisprudential debate in the Arab and Muslim World in the twentieth century. It is not surprising that the question of *riba* would come under strong scrutiny: a significant legal problem appears whenever the concept of interest falls in the purview as long as interest rates have not hit unusual ceilings, all transactions conducted in society are valid. But if *riba* is in essence defined as interest, then the whole civil and commercial structure of society becomes tainted with illegality. Mallat, C., "The Debate on *Riba* and Interest in Twentieth Century Jurisprudence" in *Islamic Law and Finance* (Edited by C. Mallat 1988 Graham & Trotman) pp. 69-88 at 69.

<sup>6</sup>Gotanda, J., "Awarding Interest in International Arbitration," *AJIL* Vol. 90 [1996] pp. 40-63 at 47.

taking interest to be void. This Article is considered to be related to public policy and can not be discarded, bearing in mind that the Yemeni Civil Code is based on *Shari'a*.<sup>7</sup>

In contrast, another ICC arbitration held in Algeria, concerned a dispute arising out of an agreement between an Algerian State company and an American company to build a railway in Algeria. Since the Algerian company did not fulfil its obligations as agreed in the agreement between the two parties, the American company sought to settle the dispute by arbitration. As a result an arbitral tribunal of three arbitrators was set up, which decided to apply Algerian law to both the merits and procedures of the arbitration, since the place of arbitration and execution of the agreement was in Algeria. The arbitral tribunal held the Algerian company liable and responsible for nonperformance of the agreement, and awarded compensation with interest to be paid by it. The Algerian company in turn refused to pay interest, on the grounds that the Algerian law, which is the applicable law, forbids awarding interest; its refusal being based on Article 1 (2) of the Algerian Civil Code, which states that in the absence of any legal provision, the judge should apply Islamic Law first then he or she could apply customs. Since Islamic law, forbids as a general rule awarding interest, the Algerian company insisted on not paying interest; in its judgment the arbitral tribunal did not take this point in account, instead it referred to Articles 182 (2) and 186 of the Algerian Civil Code, which allow awarding interest as a part of compensatory damages. As such the arbitral tribunal held on 18th of December 1985 that since there are provisions allowing awarding interest, Islamic law should not be applied in this respect.<sup>8</sup>

Another example is ICC Case No. 4604 **Parker Drilling Co. v. Sonatrach**<sup>9</sup> the arbitral tribunal in this case declined to award any interest, in accordance with Islamic Law, despite appeals to equity and general business practice, because that the general reference to Islamic law in the Algerian Civil Code meant that interest was not permitted in any context. In a different case a final award was awarded on the 20<sup>th</sup> of November 1987<sup>10</sup> which involved a pipeline contractor and an oil company, the arbitrators declined to award interest to the claimant according to the fact as they stated "*The Shari'a Islamic*

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<sup>7</sup> ICC Court of Arbitration award rendered in 26 / 9 / 1985 unreported.

<sup>8</sup> ICC Court of Arbitration Award rendered on 18 December 1985 unreported.

<sup>9</sup> Award of January 7, 1985 unreported.

<sup>10</sup> Reported Yearbook Comm. Arb'n XIII (1989) pp.47-70.

*Law expressly forbids any charging of interest because it involves usury, not chargeable in Islamic Law.”*

In another ICC case<sup>11</sup> the parties to the dispute in question submitted opinions from experts in Saudi law with reference to the question of whether, an award of interest would be prohibited by the *Shari'a* law, in their final award, the arbitrators held that *Shari'a* did not prohibit the awarding of interest, they stated that:

*“However, in order to respect the sensitivities of Shari'a law in this field, we do not consider that compensation should be awarded at a commercial rate of interest, but that it should rather be based on a rate which reflects the incidence of annual inflation over the period [at issue]. On this basis we award to claimant, by way of additional compensation for financial damages, simple interest at the rate of 5% per annum over 5 years.”*

In this respect, it is important to examine the relevant provisions in the Egyptian Civil Code of 1949 since it inspired most of Civil Codes in the Arab countries, the most important principle adopted by the Egyptian Civil Code is posited in Article 227(1): *“The contracting parties can agree on a different rate of interest, whether in return for a delay in payment or in any other situation, on condition that this rate does not exceed 7 per cent. If they agree on an interest that exceeds this rate, this interest will be reduced to 7 per cent, and any surplus already paid must be returned.”* Furthermore, Article 226 of the Code states that in case of delay after the payment is due, an interest of 4 per cent in civil, and 5 per cent in commercial, transactions will eventually be owed by the defaulting borrower. It is obvious that Article 226 allows 4 per cent interest on compensatory damage.

In the **LIAMCO**<sup>12</sup> arbitration the sole arbitrator refused to award interest of 12% as demanded by the claimant and applied instead the rate of 5% provided for by the applicable Libyan Civil Code for commercial matters, since this rate could not come into

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<sup>11</sup> Final award in case No. 7063 (1993) published in Yearbook Comm. Arb'n XXII (1997) pp. 87-91.

<sup>12</sup> 20 I.L.M. (1981) at 1.

conflict with the Islamic *riba* principle which forbids interest rates as an unjustified and usurious means of exploitation.

In an *Ad Hoc* arbitration **Pipeline Contractor (Netherlands/Saudi Arabia) v. Oil Company (U.S./Saudi Arabia)** it has been stated that “*The Shari’a Islamic law forbids usury in any form or manner whatsoever, whether or not it is gained openly or in secret, as it is said in the great Book: ‘Allah has permitted the sale of things, but not usury’.... Similarly, the messenger, may the prayers of Allah be upon him, also stated: ‘There are seven deadly sins’. They asked the Messenger of Allah, what are they? And He replied: ‘...and the taking of interest.’*”<sup>13</sup>

In 1994 the Republic of Yemen enacted the New Arbitration Act, according to Article 55 of the New Act the Court of Appeal may set aside an award on its own motion in the following cases:

- (a) if the award was made on non-arbitrable question;
- (b) if the award is against public order or the provisions of the Moslem *Shari’a*.

Having discussed objective arbitrability in relation to Islamic law and what matters could be arbitrated, the focus will be upon subjective arbitrability, briefly discuss who may enter into arbitration agreement in Islamic law.

In general, capacity is divided into two categories: (i) the capacity to dispose of a right and (ii) the capacity to exercise such a right. The necessary capacity to enter into arbitration agreement in Islamic law is that needed to dispose of one’s right. There are many factors, which effect the capacity of natural persons; the most important of which is the age of majority.

Saudi law, which serves as a good illustration of laws based on *Shari’a*, dealt with the question of arbitrability. As a general rule any dispute is arbitrable unless compromise in this dispute is not permitted. Article 1 of the Implementation Rules for the Arbitration Act provides that “*Arbitration is not permitted in matters in which compromise is not permitted, such as divorce for adultery by the woman and any thing relating to public order*”.

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<sup>13</sup> Yearbook Comm. Arb’n XIII (1989) at 47, 51.

It should be noted that Saudi law does not distinguish between civil matters and commercial matters, arbitration is not permissible for disputes relating to personal status, except disputes relating to the monetary consequences of rights relating to these disputes.

It is not possible either to refer to arbitration the following categories of disputes:

- 1-Disputes between partners of a company or between such partners and the company.
- 2-Disputes relating to commercial agency contracts.
- 3-Disputes amongst foreign contractors or companies and their Saudi sponsor.<sup>14</sup>

With regard to the capacity to arbitrate, an agreement to arbitrate may only be entered into by persons able to exercise their rights. The guardian of a minor or the administrator of a religious foundation may resort to arbitration if they have obtained the authorisation of the competent court. The same holds true for bankrupt persons.<sup>15</sup>

Another law which has been influenced by *Shari'a* is the New Egyptian Law on Arbitration No.27 of 1994. This law has adopted a wide definition of the term '*commercial arbitration*'; similar to that contained in the UNCITRAL Model Law of 1985, giving the concept 'commercial' an economic meaning. Article 11 of the new law provides that '*arbitration is not admitted in those matters which may not be subject to conciliation*'. This may raise some difficulties, since there are some matters, which cannot be subject to compromise, and yet can still be resorted to arbitration as administrative contracts; in fact, matters which can be subject to compromise and arbitrable matters are not totally identical. With regard to subjective arbitrability, and according to the same Article, agreements to arbitrate may be entered into by any natural or judicial person having the capacity to dispose of its rights, such as juristic persons of public law, who may enter into an agreement to arbitrate.

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<sup>14</sup> See Generally, El Ahdab, A., *Arbitration with the Arab Countries*, Kluwer, 1990, pp. 608-615.

<sup>15</sup> El Ahdab, A., *Arbitration with the Arab Countries*, Kluwer, 1990, p. 612.