

Legal Groundwork for the Practice of Islamic Finance in Central Europe and in the Czech Republic

The lack of knowledge about Islamic finance makes the practice much more difficult as people could misinterpret Shariah laws,, especially in central Europe. JUDr. IVANA HRDLICKOVA, Ph.D. discusses.

The European market is witnessing the growing Shariah compliant assets in the western countries, especially in the last few years. The growing Muslim population in Europe is one of the reasons, but the opportunity for entrepreneurs, for the investment is also highly significant. We can see that the situation in Europe is changing and many countries have been trying to find a solution for their economic and financial crisis; and people are observing the Islamic finance practice in many countries.

The awareness about the basic principles of the Islamic finance is very low, especially in Europe, and even many Muslims don't know how Islamic finance really works.

Contractual and legal issues

Every contract, and Islamic finance contract is not an exception, should have a real possibility of execution, otherwise it cannot be used successfully.

Does the legal framework of the central European countries cover the practice of Islamic finance? If there is an Islamic finance contract made within the central European legal framework, can it also be successfully executed? And if yes, how?

Will the European judges explain Islamic law or shall we concentrate more on alternative dispute resolutions? This question has been on the mind of many European entrepreneurs, bankers and also lawyers, who are interested in Islamic finance practice, but still don't know how this way of financing works.

The central European countries have a lot in common regarding their legal history and legal culture, and are slightly different from common law countries and also from the other European countries. If we can explore the possibilities of practicing Islamic finance in Europe, then we can take advantage of the similarity of the central European countries. Central Europe covers countries like Austria, Germany, Lichtenstein, Slovenia, Switzerland Hungary, Czech Republic, Slovakia and Poland.

There is no doubt that Islamic finance will attract more business entities and people living in central Europe. The lack of knowledge and awareness about Islamic finance makes the practice much more difficult however as these people could misunderstand or misinterpret Shariah laws. Unfortunately, the laws regarding Islamic finance have not been codified in any form.

A clear understanding of the decisions, opinions and Fatwas given by the Shariah boards of each Islamic financial institution would help the European lawyers and bankers, who are not educated in Islamic law, to deal with the Islamic finance principles.

From an international point of view, particularly in central Europe, the legal structure has been quite conservative and based strictly on written law, which may be very useful, if the international Islamic finance organizations would express some clear rules concerning Islamic finance practice as the first step to possible later codification. And even if the rules cannot be codified, it would definitely help the European experts to be more familiar with the principles and the awareness of Islamic finance principle could then increase.

This wish or a silent request can be heard from many European financial and especially legal experts, who are intending to explore the Islamic finance field. When we study the decisions of the Shariah boards carefully, we can perceive many differences. It is not an exception when two Islamic scholars do issue two different Fatwas. Although there may a reason for that, the worldwide globalization of Islamic finance practice would appreciate a greater congruence.

The Regulation Rome I has changed some principles, expressed in the Rome Convention concerning the choice of law. Nevertheless it did not make it clear enough whether it is possible to choose non-state law in the contractual obligations. The well-known UK precedent delivered in case of Shamil Bank of Bahrain against Beximco Pharmaceutical in 2004, according the Roma Convention, said that non-state law is not allowed in the contract. The legislation has been changed since then, nevertheless the jurisprudence relating to Regulation Rome I is still not unified.

Choice of law

The institute of choice of law in the Islamic finance contracts may be one of the positive solutions on how to start practice of Islamic finance within the central European legislation. The legislation of some European countries allows choosing non-state law for the arbitration.

The institute of choice of law, however, bears two ways of reasoning. The first one is to determine whether non-state law may be applicable in a contract or not. If we conclude that the non-state law cannot be applicable, then we will have to choose a state law and to consider public policy. But if the conclusion is that non-state law may be applicable in a contract, then we need to go further in determining if Islamic law may be chosen as a non-state law.

It should be clear what Islamic finance law, if chosen as a non-state law, governs the contract means and also if public policy plays a significant role. Generally, without any clarification and unification, it may not be easy to determine Islamic law as the law governing a contract in central European countries.

On the other hand, there may be a possibility in some contracts to use Shariah as a non-state law, if it is clear, internationally acceptable, offers guidance and is usable in Islamic finance contracts.

Enforcement of contracts

The enforcement of the Islamic finance contracts is also an important. The alternative dispute resolution has started playing a significant role in the central European countries as well. It may be very useful to settle the rules for the arbitration of Islamic finance contracts using the alternative dispute resolution.

The regulation of contractual obligations in the Czech Republic is governed by the Roma I Regulation (since the 18th December 2009), International private law Code Nr. 101/1963 Coll., Commercial and Civil Code. The Czech Republic as a post-communistic country has amended all the legislation relating civil and commercial transactions within last 20 years and drafted completely new legislation: including Civil Code Nr. 89/2012 Coll., Company and Corporate law Code Nr. 90/2012 Coll and International private law code Nr. 91/2012 Coll.

This legislation has been adopted already and will come into force on the 1st January 2014. This new legislation makes much more transparent beneficial ownership of the legal entities, regulates usury and introduces a new institute 'laesio enormis' (disproportionate shortening), also known in the Austrian and German legislation (and known in the old Czech legislation, valid until 1964).

The new regulation will protect the parties of a contract from using usury or high interest more than the current legislation (where using high interest and even usury is not regulated by law and the only legal framework has been enacted by the jurisprudence of the Supreme Court). The new legal framework should be helpful for the practice of Islamic finance principles.

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