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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	:	**Chapter 11**
ARCAPITA BANK B.S.C.(C), et al.,	:	**Case No. 12-11076 (SHL)**
Debtors.	:	**(Jointly Administered)**

STATEMENT OF OFFICIAL COMMITTEE OF UNSECURED CREDITORS IN SUPPORT OF DEBTORS' MOTION AUTHORIZING REPLACEMENT FINANCING AND JOINDER IN THEIR REPLY TO OBJECTION TO SAME

The Official Committee of Unsecured Creditors (the "Committee") of Arcapita Bank B.S.C.(c) ("Arcapita Bank") and the other debtors in possession in the above-captioned jointly administered chapter 11 cases (collectively, the "Debtors") hereby (i) makes a statement in support of the final approval of the *Debtors' Motion for Order Pursuant to 11 U.S.C. §§ 105, 362, 363(b)(1), 363(m), 364(c)(2), 364(c)(3), 364(e) and 552 and Bankruptcy Rules 4001 and 6004 Authorizing the Debtors to Obtain Replacement Postpetition Financing to Repay Existing Postpetition Financing* [Docket No. 1157] (the "DIP Motion"), and (ii) joins in the Debtors' *Reply in Support of Debtors' Motion Authorizing Replacement Postpetition Financing* [Docket

No. 1275] (the "Reply").[1] In connection with the foregoing, the Committee respectfully states as follows:

STATEMENT AND JOINDER

1. In its capacity as the estate fiduciary representing the interests of all of the Debtors' unsecured creditors, the Committee supports the final approval of the replacement financing requested by the Debtors and joins in the Debtors' reply to the *Second Objection of Captain Hani Alsohaibi to the Motion of First Islamic Investment Bank B.S.C.(c) n/k/a Arcapita Bank B.S.C.(c) and its Fellow Debtors for Authority to Obtain Replacement Financing From Goldman Sachs to Repay Existing Financing* [Docket No. 1261] (the "Objection").

2. The Committee, through its advisors, has been actively involved in the process of assuring the Debtors' access to appropriate debtor in possession financing throughout these cases. As is clear from the *Response and Limited Objection of Official Committee of Unsecured Creditors to Debtors' Motion to Approve DIP Commitment Letter and Fee Letter* [Docket No. 533] filed by the Committee in connection with the Debtors' initial request for authorization to enter into a commitment letter in September 2012, the Committee did not simply stand by waiting for the Debtors to negotiate with prospective lenders. Instead, the Committee and its advisors have been taking an active role in every step of the negotiation and documentation of the Debtors' postpetition financing.

3. It is on the basis of this active involvement that the Committee believes the terms of the DIP Agreement currently before the Court for final approval are appropriate and in the best interest of the Debtors' estates and creditors. Accordingly, the Committee requests that the Court overrule the Objection and approve the DIP Agreement on a final basis.

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[1] Capitalized terms used but not otherwise defined herein shall have the meaning ascribed to them in the DIP Motion and/or the Reply.

4. The arguments raised by Captain Alsohaibi (the "Objector") in the Objection are bottomed at his assertion that the DIP Agreement does not comply with *Shari'ah* law. Because of that, according to the Objector, (i) the Debtors are not authorized to enter into the DIP Agreement, and (ii) accordingly, the DIP Motion should be denied.

5. The Committee agrees with the Debtors that these objections are entirely irrelevant. The compliance of the DIP Agreement with *Shari'ah* law is not – and cannot be – before this Court. The standards for approval of DIP financing are set forth in the United States Bankruptcy Code, which does not mention *Shari'ah* compliance as a prerequisite for approval of a debtor's request for financing. As to the enforceability of the DIP Agreement, the *Shari'ah* compliance is similarly irrelevant. The DIP Agreement is explicitly governed by English (not *Shari'ah*) law. See DIP Agreement § 23.1 ("This Agreement and any non-contractual obligations arising out or in connection with it are governed by English law."). Thus, its enforceability is a matter of compliance with English law, and there is no suggestion in the Objection that it does not comply with, or is unenforceable under, English law. English courts decline to rule or comment on the compliance of a challenged agreement that is governed by English law with *Shar'iah* principles. See Shamil Bank of Bahrain v Beximco Pharm. Ltd., [2003] EWHC 2118 (Comm.), 2 All E.R. (Comm.) 849 (Eng.), aff'd [2004] ECWA (Civ) 19, 1 W.L.R. 1784 (Eng.), attached hereto as "Exhibit A."

6. As to the Objector's argument that Arcapita Bank B.S.C.(c) (the "Bank") is not authorized to enter into the DIP Agreement, it is based on a faulty factual premise. The Bank is ***not*** the Purchaser under the DIP Agreement, AIHL is.

7. In any event, the Committee and its advisors believe that the DIP Agreement is, in fact, *Shari-ah*-compliant. As the Objector himself acknowledges, all that the CBB prescribes to ensure such compliance is the vetting of the proposed financing transaction by

a *Shari'ah* Supervisory Board. Objection ¶ 42 (citing CBB rule HC-9.2.1). The Debtors clearly have complied with that requirement. In addition, the structure implemented by the Revised Finance Agreements is consistent with precedent *murabaha*-based financings widely used in the Islamic finance sector. To the extent a single disgruntled creditor disagrees with the Supervisory Board's determination, this Court clearly does not have the jurisdiction (or any need) to resolve such dispute.[2]

8. What the Court clearly does have the jurisdiction and the need to determine, however, is the potentially devastating effect that the non-approval of the DIP Motion on a final basis would have. The Debtors are about to exit from chapter 11, having confirmed the Plan that was overwhelmingly supported by all parties in interest. But without the necessary funding to allow such Plan to be consummated, all the hard work of the Debtors and the Committee to achieve the confirmation of the Plan would go to waste. See *Confirmed Second Amended Joint Plan of Reorganization of Arcapita Bank B.S.C.(c) and Related Debtors Under Chapter 11 of the Bankruptcy Code (with First Technical Modifications)* [Docket No. 1265] § 10.1.2.5 (specifying that a condition precedent to the Effective Date is that "[t]he documents evidencing the Exit Facility shall have been executed and delivered by the respective parties thereto, and all conditions precedent to the effectiveness of such documents shall have been satisfied or waived").

9. Finally, despite the Court's explicit finding at the June 10, 2013 interim hearing that the relief requested in the DIP Motion has been well-noticed (See Hr'g Tr. 22:13-23 (June 10, 2013)) [Docket No. 1276], the Objector continues to press his procedural argument of insufficient notice. The changes effected by the Revised Financing Agreement do not impact the

[2] Interestingly enough, despite having first appeared in these cases in September 2012 when he filed a *pro se* motion to dismiss the chapter 11 cases, Docket No. 525, the Objector took no issue with similarly structured transactions, including the Fortress Facility and the SCB Facilities, on the basis of nonconformity with *Shari'ah* principles or otherwise.

basic structure of the DIP Transaction, accordingly, the Court's prior ruling on the adequacy of notice stands.

10. For the foregoing reasons as well as those contained in the Reply, the Committee respectfully requests that the Court (i) overrule the Objection, (ii) approve the DIP Agreement on a final basis, and (iii) grant all other relief requested in the DIP Motion.

Dated: New York, New York
June 20, 2013

MILBANK, TWEED, HADLEY & McCLOY LLP

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Exhibit A

Shamil Bank of Bahrain v Beximco Pharmaceuticals Limited and Others

2002 Folio No 1172

High Court of Justice Queen's Bench Division Commercial Court

1 August 2003

Neutral Citation Number [2003] EWHC 2118 (Comm)

2003 WL 22187542

Before: Mr Justice Morison

Friday 1st August 2003

Representation

Ms Sara Partington (instructed by Norton Rose) appeared on behalf of the Claimant.

Mr Richard Hacker QC (instructed by Jaswal Johnston) appeared on behalf of the Defendants,.

APPROVED JUDGMENT

MR JUSTICE MORISON:

1. This is an application for summary judgment by the claimants, the Shamil Bank of Bahrain EC (the bank). The bank is incorporated under the laws of Bahrain and is authorised to act as such by the relevant authority; namely the Bahrain Monetary Agency. It operates in accordance with the principles of Sharia'a law as an Islamic financial institution. Its commercial activities are supervised by its religious supervisory board to ensure that they are conducted in accordance with the Sharia'a principles. The board comprises distinguished Islamic scholars from Egypt, Turkey, Saudi Arabia and Bahrain.

2. It is not in dispute that the board has certified the activities of the bank, which include the transactions giving rise to the present dispute, to be in compliance with Sharia'a law. Nor was it suggested, until the defence was filed in this action, that the defendants were dissatisfied, on religious grounds, with the arrangements agreed between the parties.

3. The first two defendants are companies incorporated in Bangladesh involved in the manufacture of pharmaceuticals and in export and import trade, respectively. The third and fourth defendants are directors of the first two defendants and of the fifth defendant, which is the parent of the first two.

4. The transactions between the parties may be summarised in this way. After some negotiations, in 1995 the bank and the first two defendants entered into a Morabaha Financing Agreement. The structure of the agreement was that the bank were described as the seller and the first defendant the buyer. The second defendant was appointed by the bank as its agent "for the purchase of the goods" by the bank. The first defendant agreed to buy the goods from the bank and to pay the bank the Morabaha price. The price included a profit element.

5. Effectively, the bank were advancing funds to the defendants and repayments including profit were to be made over a period. The parties conferred on this court, jurisdiction over any legal action or proceedings "arising out of or in connection with this agreement" and the parties' choice of law was expressed in this way:

> "Subject to the principles of Glorious Sharia'a, this Agreement shall be governed by and construed in accordance with the laws of England."

6. On the same date, 28th December 1995, the parties separately agreed an agency contract between the bank and the second defendants which identified the bank's contribution towards the costs of the goods to be purchased as US $15 million.

7. A payment schedule forming part of the Morabaha Agreement was also agreed which identified the number of instalments and their amounts. Repayment was to commence on 28th March 1996 and the last payment of US $15,323,322 was due on 28th December 1997 making a total repayment of US $17,586,583 million.

8. Also on the same date, the parties entered into a market rate agreement.

9. On 3rd January 1996, the claimants paid the second defendants 15 million and, in accordance with the Morabaha Agreement and the schedule of repayments, the first defendant paid 7 instalments each of US $323,323 leaving only the payment of the last instalment.

10. The parties entered into a second Morabaha Agreement whereby the bank extended a further facility of US $15 million to the second defendant. Its terms, and the repayment terms, were essentially the same, However, the first four instalments were of relatively small amounts between US $367,500 and US $375,667. The fifth, sixth and seventh instalments were somewhat larger: about US $2.8 million each and the last payment was 7.6 million odd making a total repayment of US $17,609,932. Between 15th October and 12th August 1997, the second defendants paid the four smaller instalments.

11. Admittedly, the first two defendants defaulted on the agreements and, following discussions, they entered into new arrangements, which I shall call the “exchange agreements”. These agreements, which were entered into on 14th September 1999, were amended on two separate occasions: first on 4th February 2001 and again on 30th January 2002. The original exchange agreement, dated 14th September 1999, recited that there was owing to the bank, under the first Morabaha Agreement, an outstanding amount of US $15.323,323 million together with “accrued compensation” for failure to pay sums on their due dates. The substance of the new agreement was that the personal and corporate guarantors were released, from their obligations and the bank would discharge the outstanding amount in consideration of the first and second defendants transferring to the bank certain identified assets which, subject to conditions, the defendants would be entitled to use until 31st December 2002. For their use of the assets, the companies were required to pay a user fee. The guarantors were to enter into new personal guarantees. There was an identical governing law clause, to that in the Morabaha Agreements; the parties to the original exchange agreement were simply the bank and the first and second defendants.

12. On 4th February 2001, what was described as a supplemental agreement was made between all the parties to this action and an entity called New Dhaka Industries Limited, another Bangladesh company. This agreement also recited that the changes were being made at the request of the first and second defendants. The new agreement provided for the giving of personal guarantees by the third and fourth defendants and their guarantees, entered into on 6th February 2001, obliged them to pay all monies and discharge all obligations and liabilities now or hereafter due, owing or incurred by, the first and/or second defendants.

13. The guarantee contained a law and jurisdiction clause:

> “This guarantee is governed by and shall be construed in accordance with English law.”

The guarantors irrevocably and unconditionally submitted to the jurisdiction of the English courts, although the bank were also free to take proceedings against them in any one or more other jurisdictions. On the same day, the fifth defendant entered into a guarantee in the same terms.

14. The bank say that, as at the effective date, namely 4th April 2002, there were outstanding, under the two Morabaha Agreements, US $28,442,838 together with accrued compensation of US $3,031,710.52. Under the exchange agreement, the bank are regarded as having discharged the outstanding amount and there upon, the first and second defendants were obliged to commence payment of the instalments of the user fees. The total amount of the user fee was US $46.860 million. Because the user fee was not paid, the bank exercised their right to accelerate the repayment of all user fees (see the letters of default referred to in paragraphs 8.1 and 8.2 of the points of claim). As at the date of the proceedings, the defendants owe them $49,711,710.52 million plus such compensation ‘as the court may determine for such periods as it thinks fit.’. To the letters of demand,

there was no response and the proceedings were commenced in this court on 8th November 2002.

15. The amounts being claimed, as such, are not in dispute but the defences which have been advanced are as follows:

(1) Because of the wording of the governing law clause, that is:

"Subject to the principles of Glorious Sharia'a this agreement shall be governed by and construed in accordance with the laws of England",

the obligations are only enforceable if they are enforceable both under Sharia'a law and under English law. Because the agreements provide for the payment of "interest" or "Riba" they are not enforceable under Sharia'a law. Whilst the defendants accept that they received the advances, neither party:

"was under any illusion as to the commercial realities of the transactions".

The loan was "dressed up" as a Morabaha sales or Ijarah leases. They were merely "a disguise for an otherwise undocumented interest bearing loan". They say that both the accrued compensation payments and the rolling over process involved in the exchange agreements offended Sharia'a law, as did the acceleration of payments provided for under the exchange agreements.

(2) Regrettably, the defendants say, the loans could not be repaid and more time had to be sought from the bank. The exchange agreements were designed to ensure that the repayments could be achieved in accordance with the defendants' cash flow position, but they were unable to meet the schedules; and thus an oral agreement was made, under which the bank agreed to stay their hand and agreed that the debt would be suspended, until the parties had agreed upon a restructuring of the debt. As yet, no such agreement had been arrived at and thus the debt cannot be called in, as it is not due for repayment.

(3) The bank is estopped from claiming the monies because it represented that it would not seek to recover them until the defendants had agreed the restructuring of the debts.

(4) The guarantees are not enforceable because the bank had no capacity to enter into them, under Bahrain law, which applies to determine the capacity of the bank to enter into such a transaction, as that is the law of the place of its incorporation.

(5) They were also not enforceable because the guarantees are void for mutual mistake. The guarantees were executed at a time between the first variation to the exchange agreement and the second and final variation. The effect of these variations was to postpone the date on which the bank became liable to discharge the borrowers' "outstanding obligation to pay the outstanding amount under the 1995 and 1996 agreements". Accordingly, the guarantees were given at a time when both parties believed that very substantial sums remained due, under the 1995 and 1996 Morabaha and market rate agreements. Those agreements were void and unenforceable under the Sharia'a principles. Both parties were unaware of that fact when the guarantees were executed. There was no commercial rationale for the guarantees (which recorded as the consideration the promise by the bank to discharge the outstanding amounts due under the 1995 and 1996 agreements) if no such amounts were due. If the bank seeks to rely on a clause in the guarantee whereby the guarantors assume primary responsibility, in the event that any obligation of the bank were unenforceable for any reason, this would constitute "a disguised attempt, indirectly, to enforce obligations which are tainted by unlawfulness under their proper law".

16. This is not the occasion for a mini trial. Either the defences are credible or they are not. I am not obliged to accept the truth of everything put before me, but there is a blurred line between my being sceptical about the truth of what I am told at this stage and being persuaded that what I am told can be categorised as improbable or fanciful.

17. In the most general terms, the defences have all the hallmarks of being trumped up. There is no doubt that the bank advanced monies to the first two defendants and that these monies have not been repaid. No "religious" point was made until the defendants were sued. The concept of an oral agreement, which postpones the date for repayment until the parties reach a further agreement, which may be in the distant future, seems improbable in the extreme. Estoppel and mutual mistake are often the bed fellows of a well advised, desperate litigant who is scraping the barrel to avoid obligations.

18. The court's initial scepticism is enhanced by knowledge that the defendants are submitting that the:

> "Factual basis of certain of the defences raised (collateral agreement/promissory estoppel) substantiates the defendants' case that they do not have the means to make a payment of $28.4 million into court (whether within 14 days or at all)".

19. But I must examine the defences with care because an instinctive approach to the issues is not sufficient or appropriate. I start with the point that is made that the claims asserted by the bank are unsustainable under Sharia'a law. The first question is whether the words "subject to the principles of Glorious Sharia'a" mean that in order to be enforceable, the agreements must both be valid under English law and under Sharia'a law, as the English court may find it to be. The claimants do not accept this proposition. One of the points they make is that there is no such thing as a recognised law of Sharia'a. A considerable amount of evidence has been adduced, from experts on either side, as to Sharia'a law and the lawfulness of the arrangements with the bank, under Sharia'a law, which I am told is the same as Islamic law.

20. The defendant's case on Sharia'a law is that:

> 1) Here, there is a coherent logical and credible explanation of why the fundamental claims asserted in this case are "unsustainable under Sharia'a law".
>
> (2) The bank being incorporated in Bahrarn was established for the purpose of providing finance and banking services which are consistent with, and do not conflict with, Sharia'a law. The principles of Sharia'a law preclude the charging of Riba. More particularly, the principles of Morabaha Agreements are that the form of transaction is apt only to fund the purchase of specific goods and not for general working capital. In this case, the evidence shows that the monies were never intended to be used for the purpose of purchase of specific goods, to which the bank obtained title. Therefore, it is unenforceable and that this would be so whether or not the bank was aware of what the defendants were going to do with the money. Although they say, in this case, that the bank was well aware of the position. They say that the obligation to pay further accrued compensation, in the event of delayed payments under the Market Rate Agreement "plainly offend the principles of Sharia'a". They further say that: in relation to the exchange agreements, these constitute loan agreements which appear, in form, to constitute a legitimate recognised and acceptable source of Islamic finance, namely ijarah or lease. However, in substance, these agreements do not achieve Sharia'a compliance because the bank did not take title, or the right of usufruct, to the goods purportedly leased. Secondly, they simply constitute a rolling over, or rescheduling, of the Morabaha arrangements themselves, not being in conformity with Sharia'a law.

21. The claimants say the bank's commercial activities are supervised by the religious supervisory board, to which I have made reference. They say that the role of the board is described in the bank's

memorandum and articles of association. Paragraphs 35 and 36 of the bank's Articles of Association. To be found in bundle 2 page 402.

> “The Religious Supervisory Board shall ascertain that the Company's investments and activities (and the activities of its subsidiary and affiliated companies) conform with the principles and provisions of Islamic Sharia'a. It shall, in particular, discuss with the members of the Board of Directors, managers of the Company or of any subsidiary or affiliated company under its control, such conformity and the business carried out by them and shall request any information it deems necessary. In particular, the Religious Supervisory Board shall adopt all the crucial decisions for applying the provisions of Islamic Sharia'a to ensure the realisation of the objects for which the Company was incorporated. Also, to ensure that the members of the Board of Directors, managers and employees are co-ordinating their activities according to such decisions which shall be binding upon all the shareholders. The Religious Supervisory Board shall within six months from the end of the Company's financial year, submit a written report stating that it fulfilled the obligations indicated herein and ascertained that the Company's investments and business activities (including its subsidiary companies) conform with the provisions of Islamic Sharia'a.
>
> The Religious Supervisory Board shall appoint — upon the nomination by the Chief Executive — a Sharia'a Supervisor who shall act as the Secretary of the Religious Supervisory Board. He need not be a member of the Religious Supervisory Board.
>
> The Board of Directors shall take the necessary actions to ensure that all the investments and other business transactions have been referred to the Religious Supervisory Board for approval before carrying out any other business transactions by the Company or by any subsidiary or affiliate company under its control.”

(2.22 pm)

22. At the end of each year, the religious supervisory board certify that they are satisfied that the transactions of the bank are considered by the board to be in compliance with Sharia'a principles. The board, as I have indicated, compromises distinguished Islamic jurists from a variety of countries and the religious supervisory board is appointed by the bank's shareholders.

23 The claimants also say that the words “subject to the principles of Glorious Sharia'a” do not constitute a choice of law at all but are a reference to, or a reflection of, the fact that the bank seeks to conduct its affairs according to Sharia'a principles under the supervision of the board. They also say that even if Sharia'a law were to apply, then in accordance with the opinion of Dr Lau, their expert, the exchange agreements, under which these claims are made, are enforceable. They say, in any event, if they are wrong about all that, at least the capital that has been advanced by the bank is due and owing under the exchange agreements even if the compensation and other amounts on top are not.

24. They say that the words “Glorious Sharia'a principles” are a reference to religious principles rather than to a choice of a coherent system of law. There is, they submitted, the greatest controversy, as shown by the evidence, between experts and indeed between Islamic courts, as to the “true” principles. And, given that controversy, it is highly improbable that the parties intended an English court to determine difficult questions of the Sharia'a principles. As Dr Lau points out in his first expert report, Sharia'a law is made up of conflicting pronouncements and there is a considerable debate as to what is and what is not permissible under it. The situation is complicated by the fact that much of the classical law emerged at a time when many financial concepts simply did not exist. It is because of these systemic uncertainties and controversies that Islamic banks submit themselves to the supervision and scrutiny of religious supervisory boards.

25. It was submitted that this statement is supported, to an extent, by the fact that Mr Justice Khan's confident assertions, as to the principles of Sharia'a law, were overruled, effectively, by the Sharia'a appellant branch of the High Court of Pakistan which annulled his judgment in the Khaki case. It is also, they say, supported, to an extent, by Mr Justice Khan's report itself.

> “In the Sharia'a, there is no opinion of any person, body or jurist which binds a court which has to decide a Sharia'a issue. The dispute must be resolved by the court in the light of its' own view of the position under Sharia'a law.”

26. These issues, says Mr Doctor on behalf of the claimants, are significantly not left to the ordinary civil courts to decide in Pakistan, which is attempting to Islamicise its banking and financial laws. Therefore, it is inconceivable, or perhaps just unlikely, that the parties in this case intended that the English secular court be entrusted with the task of deciding between opposing points of view which themselves may be based on geopolitical and particular religious beliefs. Each opposing jurist might be equally right. His opinion might be equally valid and sustainable. There is no guarantee that either party would be prepared to accept the ruling of an English secular court on this subject.

27. Mr Doctor also drew attention to article 3.1 of the Rome Convention which applies by virtue of article 1.1. Article 3 of the Convention provides:

> “A contract shall be governed by the law chosen by the parties. The choice must be express or demonstrated with reasonable certainty by the terms of the contract or the circumstances of the case by their choice, the parties can select the law applicable to the whole or a part only of the contract.”

In this case, it is clear that the parties chose English law to be the governing law of the agreement. Dicey and Morris note, at paragraph 32–079, that:

> “Article 1.1 of the Rome Convention makes it clear that the reference to the parties' choice of ‘the law’ to govern a contract is a reference to the law of a country. It does not sanction the choice or application of a non-national system of law, such as the lex mercatoria, or general principles of law.”

Counsel also referred, in his written argument, to a passage in a book called: “The Conflict of Laws” by A Briggs, the 2002 edition, at page 159:

> “A choice of the lex mercatoria or the laws of mars, not being a law of a country, cannot be upheld because the convention sanctions only the choice of the law of a country and, in such a case, article 3 cannot apply.”

Mr Doctor further submitted that the convention is binding on all who litigate in England, whether as claimant or defendant, and particularly it applies to those who have consented, as here, to the jurisdiction of the English courts. It is not possible to contract out of the Rome Convention. He went on to submit that this does not mean that the parties cannot incorporate, by agreement, special provisions that are suggested by, or consonant with, religious or other moral principles. But they cannot require, he submitted, the English court to adjudicate their contractual disputes according to such principles independently of the national law which is otherwise, by operation of the Rome Convention, binding on the parties to the contract.

28. In any event, the Rome Convention will not permit a situation where two laws simultaneously govern the question of the enforceability of a contract. It is true that the Rome Convention allows for the splitting of a contract so that parts of it can be governed by different laws (see the wording of article 3.1). Dicey and Morris describe the concept of, and the application of, different laws as follows:

> “The concept of depecage (or dismemberment) is used in two distinct ways in the conflict of laws. The first expresses the idea that not all issues arising out of the contractual relations will necessarily be governed by the same law: thus, while the law chosen by the parties may govern the validity of the contract, matters of form may be governed by the place of contracting, matters of capacity by the personal law and so on. The second expresses the thought that different laws may apply to different parts of the contract. The parties may stipulate (or the courts may hold) that one obligation is governed by the law of state A and another is governed by the law of state B.”

But depecage does not sanction the application of different systems of law to the same issue. There is a further quotation from Dicey and Morris:

> “There is no objection in principle to different parts of the contract being subject to different laws for the purpose, for example, of interpretation: it is in theory possible (although in practice inconvenient and inevitably rare) for one part of a contract to be

> construed in accordance with the principles of English law and for another part to be construed in accordance with the principles of French law. But there is an objection in principle to what has been called 'the general obligation' of a contract being governed by more than one law. Even if different parts of a contract are said to be governed by different laws, it would be highly inconvenient, and contrary to principle, for such issues as whether the contract is discharged by frustration or whether the innocent party may terminate or withhold performance on account of the other party's breach,' not to be governed by a single law.

(2.35 pm)

29. Mr Doctor refers to the report of Giuliano and Lagardes at paragraph 59 of the claimant's written skeleton argument.

> "Nevertheless when the contract is severable the choice must be logically consistent, ie it must relate to elements in the contract which can be governed by different laws without giving rise to contradictions. For example, an 'index-linking clause' may be made subject to a different law; on the other hand it is unlikely that repudiation of the contract for non-performance would be subjected to two different laws, one for the vendor, and the other for the purchaser. Recourse must be had to Article 4 of the Convention if the chosen laws cannot be logically reconciled."

30. It is common ground by concession that there cannot be two governing laws and reference at this point should be made to the case of American Motorists' Insurance Company v Cellstar Corporation and Another (2003) EWCA civil 206, at paragraph 32.

31. Mr Doctor made detailed submissions relating to the other two points made on Sharia'a law by the defendants, namely, that if Sharia'a law applied, the agreements did not offend it and the capital sums would, in any event, by repayable under the agreements.

32. In my view, if the court were to be concerned with the application of Sharia'a law and its impact on the lawfulness of the agreements, I would conclude at this stage that it was arguable which of the two parties' experts is right and that it would offend the principles underlying part 24 to seek to resolve them before a trial.

33. The same applies to the second argument, namely the repayablity of the capital sums. Whilst there are passages in Mr Justice Khan's report which suggest that an agreement which is in conflict with Sharia'a principles will not disentitle the lender to recover at least the principal sums advanced, this issue would also require further examination. There is, at present, no quasi contractual claim (for money had and received) or unjust enrichment and there is a sufficiently arguable case as to whether under a contract which (in the event) is held to conflict with Sharia'a law, there can be recovery of any sum at all.

34. And so I turn to the question of whether the defendants can show an arguable case that the words "subject to the principles of Glorious Sharia'a" in the context of the clause as a whole, and against the background to which I made reference, would require the court to determine what Sharia'a law was, in the relevant respects, and if not lawful by Sharia'a law but lawful under English law to conclude that the claims are unenforceable.

35. In my view, Mr Doctor is right on this issue largely for the reason which he advances in support of his argument, to which I have made extensive reference. Although Mr Hacker denies it, the case he advances amounts, I think, to a retreat from his concession, inevitably and rightly made, that there cannot be two governing laws. Effectively, he is saying that English law will not determine the enforceability of the agreement; that is an issue for Sharia'a law or for Sharia'a law as well. Mr Hacker sought to liken the clause to a clause which incorporates matters such as the Hague Rules. Of course, a contract governed by English law may incorporate rules such as those, but clear words would need to be used to produce the startling result for which he contends. At one stage, he submitted that the parties intended to subject the enforceability of the agreements to due compliance with Sharia'a principles "over and above" English law but that is not what I think the clause says.

36. Looking at the background, it seems to me clear that it cannot have been the intention of the parties that it would ask this secular court to determine principles of law derived from religious writings

on matters of great controversy. Just as I accept there is a genuine conflict of view between the experts, I reject Mr Hacker's submission that, effectively, Dr Lau agrees with what Mr Hacker calls the basic rules of Morabaha and Ijarah. There is clearly great controversy as to the strictness with which principles of Sharia'a law will be interpreted or applied. The English court, as a secular court, is not suited to ascertain and determine highly controversial principles of a religious based law and it is unlikely that the parties would be satisfied by any such ruling; that is not what they were wanting by their choice of law clause.

37. The Rome Convention strongly supports this argument. The lex mercatoria, or general law of merchants, is a law to which some international arbitral tribunals have regard but it is not the law of a country which is capable of ascertainment by expert evidence from practitioners in the country. This court, obviously, is well used to disputes about foreign law and, if necessary, it will determine what a judge in a foreign court would decide had he received submission about Islamic law. That is not the same exercise as determining what, as a matter of English law or applying English law principles, the principles of a religious based law are. Further, I see a distinction between an English court deciding whether, having regard to Islamic religious law principles, a child of separated parents should be required to undergo circumcision or not.

38. Sharia'a principles are not simply “principles of law” but are principles which apply to other aspects of life and behaviour. Sharia'a means, I am told, orthodox. Sharia'a law is the law laid down by the Qur'an and the Sunna which contain the sayings, teachings and actions of the prophet Mohammed) and the only way to know this is through the collection of Ahadith which consists of reports about the sayings, deeds and reactions of the prophet.

39. Whilst in one sense this court will answer any question posed of it, however difficult, it is improbable, in the extreme, that the parties were truly asking this court to get into matters of Islamic religion and orthodoxy. This is a especially so when the bank has its own religious board to monitor the compliance of the bank with the board's own perception of Islamic principles of law in an international banking context.

40. So far as the bank was concerned, that is likely to have been sufficient for its own regulatory purposes and there is no suggestion that the defendants were in any way concerned about the principles of Sharia'a law either at the time the agreement was made or at any time before the proceedings were started. The Sharia'a law defence is, I think, a lawyers' construct but, for the reasons I have given, in my view it does not work.

41. I turn to the second head of defence, namely what I would call the agreement point.

(2.43 pm)

The evidential basis for this alleged agreement is to be found in paragraph 42 of Mr Chowdhury's first witness statement, he being a director of the first and second defendants:

> “During this visit we had free and frank discussions with Mr Abul and his team and explained our problems relating to cash flow as well as the political problems we were facing at that time. He was very sympathetic but explained his problems, and requested us to help resolve his problems relating to the Auditor and regulatory bodies. He impressed upon us that all the paper work relating to the Supplemental Agreement had to be completed to avoid provisioning in their accounts. This should require updated BOI (Board of Investment) permission and signing side letters prepared by their legal advisers and so on. He then requested that we also make a token payment of US $500,000 to give credence to the documents prepared. (My notes of that meeting are attached at page 143 of OKC1). Then we had all the documents signed (See also para 40) and gave two post dated Taka cheques totalling equivalent US $500,000 to them. This was done as explained above solely to help them convince their auditors and regulatory bodies even though we were cash strapped. As part of this discussion he promised that, as we were helping them out, once this immediate problem was resolved, we need not pay any more amounts until a monthly agreeable long term rescheduling had been agreed. I understood that this was a formal agreement on the Claimant's part. We certainly would not have signed the documentation had the Claimant not agreed this. Although there was no specific mention of the guarantees, it was implicit in the discussion that the Claimant would not try and obtain payment from any source until the rescheduling had been agreed.”

42. This evidence is reflected in paragraphs 39 and 40 of the amended defence, which reads:

> "On 29th January 2002 a meeting was held between (amongst others) the third defendant and Mr Chowdhury on behalf of the defendants Juma Abul, Sarfraz and Maaz Khairuddin of the claimant, at which discussions in relation to the restructuring of the debt took place."

Paragraph 40:

> "It was agreed that the parties would continue their past efforts to seek to achieve a mutually acceptable agreement in relation to such a restructuring and it was agreed that, until such a restructuring had been agreed, the first and second defendants' obligations to pay the debt should remain suspended."

43. Mr Doctor says that there is a difference between the way the agreement is spelt out in Mr Chowdhury's witness statement and in the passage of the defence, which I have just referred to, but I shall overlook any difference for present purposes.

44. The effect of the agreement was to put into indefinite suspense, the bank's right to recover any sums due unless and until the defendants' finances were restructured in a way acceptable to them and to which they were prepared to agree. In other words: no further agreement, no repayment. That would be a remarkable agreement for any commercial organisation to make. It would defy both reality and common sense. Nonetheless, Mr Hacker submits that I should regard this part of the case as genuine and not either improbable (justifying a payment into court) or fanciful (justifying its rejection as a potential defence).

45. Mr Hacker submitted that there were four good reasons for this submission: first, he said there was a clear indication that, at the relevant time, the bank was in financial difficulty. Second, if the indebtedness in the present case was written off, that would have eliminated 25 per cent of the bank's net equity. Third, on 4th February 2001, when the exchange agreements were negotiated, four post dated cheques were handed to the bank in the sum of US $3 million yet they were never presented for payment. The defendants say that these cheques were asked for by the bank so that they could be shown to the bank's auditors who were shortly to sign off on the bank's accounts. Four, it appears that the bank were prepared to extend the repayment dates under the exchange agreements by one year, without effectively, any consideration.

46. In my view, none of these points is convincing. The evidence which the defendants rely on shows that the bank was required, by their national regulator, to provide shareholders' guarantees in relation to the bank's exposure in Pakistan and Indonesia. Such a requirement might have been for financial or other regulatory reasons. The bank's audited accounts do not support the contention that the bank had any financial difficulties. As at 31st December 2001, the claimants had total assets of US $2.36 billion. Its owners' equity net assets was US $242 million. If the entire amount of the defendant's debt had to be written off in January 2002, there would have still been an excess of assets over liabilities in a sum of around US $200 million and total assets of about US $2 billion; its solvency would be completely unaffected by the defendants defaulting and disappearing.

47. The post dated cheques were, so I was told by Mr Doctor and accept (the defendants served their evidence late) accompanied by a requirement that they should not be presented for payment until the defendants indicated that they had funds to meet them and that despite many requests, such indication was not given. If the cheques were given to deceive the auditors then such a deception was not likely to work since, presumably, the auditors would have been quite capable of discovering that the cheques which had been shown to them had not in fact been paid or presented. In relation to extending credit facilities for a further year, it is common ground that the claimants obtain some consideration for this.

48. The picture is clear, from the contemporaneous correspondence: it is of a claimant bank who has advanced monies seeking to chase repayment and extending time to accommodate a defaulting client. I refer in particular to two letters: the first is dated June 5th and is to be found in bundle 6 at page 1474. In that letter, the bank is chasing payment. It notes that the defendants are seeking yet further time. The bank states:

> “However, we have been more than generous in our dealings (with the defendants) in the past and are not prepared to agree to any further rescheduling. As was made clear in our letters of 9th April, 15th April and 3rd June, we expected payment of the first instalment of the user fee on 10th April and of the accrued compensation by no later than 4th June, in accordance with the terms of the agreements. In view of your breaches, please note that the bank reserves its right to take whatever action it deems necessary.”

Second, there is a letter dated 11th July from one of the two personal defendants addressed to Mr Abul who is the head of remedial management at the claimant bank:

> “We refer to your letter of 5th June and are surprised and disappointed to note that you are not agreeable to reschedule our loan. You will recall that when you visited us in January 2002, you requested us to sign a new supplemental agreement, number 2, in order to avoid classification of the loan in your 2001 balance sheet. You also requested us to obtain BOI permission on the basis of new agreement. This agreement you asked us to sign with the date of 30th January 2002, although the agreement was signed in March. At that time, you told us that the bank would reschedule our loan appeal provided we executed the above documents. Over this assurance, we agreed to execute the documents you requested. Your bank approached us through our friend, the former vice-chairman of [another company], to sign new documents as per your request to help you resolve your problems.
>
> We reiterate that we have already paid you US$11.3 million out of total compensation of US$14.3. We have fully securitised your loan and paid you all the rescheduling fees amounting to more than US$600,000. As mentioned in our letter of 23rd May, we need some time because of our present liquidity crisis but we are trying our best to pay you some compensation. We assure you that by September we will pay a substantial amount of overdue compensation. We would again request you to reschedule our loan and give us time to pay the overdue compensation.”

On 26th August 2002, the defendants sought a meeting with senior people within the bank to discuss the issue of late payment and the future repayment schedule. The closest the defendants came to mentioning the alleged agreement was in their letter of 11th July but what was said was quite inconsistent with them believing that there was no liability on them to make any further payment because of an agreement. Rather, it was the preamble for them asking for yet more than time. In commercial terms, the alleged agreement makes no sense. Had it been made, I would have expected it to have been recorded in writing; it was obviously important to a defaulting debtor and I would have expected some early reference to the agreement as an immediate response to the bank's pressures and demands. Instead, the reference to the agreement appeared for the first time in the defence.

49. I regard this defence as fanciful and with it also the defence of estoppel. I do not believe that any agreement or representation was made having regard to the facts and matters to which I have made reference. Merely because the contrary has been asserted in the witness statement, I am not required to accept it if it is, as I believe it to be, quite incredible.

50. I turn therefore to the question raised under the guarantees Mr Hacker says that the guarantees are void because first: the bank did not have the capacity to enter into them, capacity being a question to be decided exclusively by Bahrain law. Secondly: they are void for mutual mistake, and he draws the court's attention to the relevant principles set out in the case of Associated Japanese Bank v Credit Du Nord reported at 1989 one weekly law reports page 255 at pages 264 C to 269 B. And Great Peace Shipping v Tsavliris Salvage Limited reported at 2003 Queen's Bench 679 at paragraph 73 to 161 And thirdly since the underlying obligations are void or illegal, the guarantees are void and should not be enforced

51. I turn to the first point, which is supported by the evidence of a Bahrain law expert, Mr El Nayal. I am afraid that this opinion does not stand up to scrutiny. The essence of his opinion is based upon article 185 of the New Commercial Companies Law (decree law number 21 for the year 2001). At paragraph 24 of his report, the learned author makes reference to what he says are the Memorandum and Articles of Association of the claimants “which has been provided to me”. He does not produce the document provided to him, which I gather was not provided to him by the defendant's lawyers in this country. He quotes from this document, but the true memorandum and articles of association of

the bank have been produced in evidence, and I have already referred to them, and they do not contain the words to which this person is making reference. But he continues, at paragraph 25 and through to 27, to express his opinion:

> "The Claimant, being a company organised under the laws of the Kingdom of Bahrain, is under a prime obligation to perform its objects in accordance with its Memorandum and Articles of Association. The principal object of the Claimant under its Memorandum and Articles of Association is to undertake financial and banking transactions in accordance with Islamic Sharia'a. This is also a duty imposed upon the Claimant under the Law (Commercial Companies Law) the circulars and ministerial orders/resolutions read with the Governance Standards for Islamic Financial Institutions issued by AAOIFI. Under the laws of Bahrain the Claimant has no capacity to enter into any financial and banking transaction or any other business activity which is beyond the scope of its principal object. Any transaction entered into by the Claimant which is contrary to its principal object shall be null and void in the laws of Bahrain. It is a prime obligation of the Directors to comply with the provisions of the Memorandum and Articles of Association of the company. Article 185 of the New CCL reads as follows:
>
> 'The chairman and the other members of the board of directors shall be liable to the company, the shareholders and the third parties for acts involving betrayal of trust, misuse of power, breach of the law or breach of the Articles of Association of for their mismanagement of the company. Any provision in contravention of the foregoing shall be deemed null and void.
>
> Any proposal of the general meeting intended to exonerate the board of directors shall not avail against instituting an action of liability against the board.'
>
> 26. It may be noted from the above provision that an act committed by a company, through its directors or any other employee through his/her authority to act for the said directors in breach to the Memorandum and Articles of Association of a company, is deemed to be an act committed in violation of the Law as per the express provisions of the above Article. Therefore, by virtue of this Article (Article 185) if a transaction has the effect of breaching the Law or breaching the Articles of Association, then the transaction is null and void. The liability of the Directors and/or their agents acting on their behalf extends also to the third parties and it is not limited to the company and shareholders."

52. He is there saying that, by virtue of Article 185, if a transaction has the effect of breaking the law or breaking the Articles of Association, then the transaction is null and void and the bank had no capacity to enter into it. But, with very great respect to this person, it is plainly obvious from the extract of the Article 185 that he has misinterpreted it. The only way that that Article can be read is that it is saying that any provision which seeks to exclude liability to the company, of the board, shall be deemed null and void. His whole thesis on the question of capacity is therefore fundamentally flawed and a trial is not required in order to establish what is obvious. The guarantee is governed by English law and I can see no reason, in principle or law, why it should not be enforced, in accordance with its terms, including the provision that, if the underlying obligations are void or unenforceable, the guarantors remain liable as principal debtors.

53. In the light of my other findings, that is sufficient to dispose of the first head of defence to the guarantee. As to mistake, because I have rejected the argument that, subject to the provisions of Glorious Sharia'a, has the meaning contended for, this defence does not arise but, if it did, it seems to me that a common mistake as to the legal consequences of an agreement would not qualify as a mistake apt to give rise to a defence in any event.

54. The third guarantee defence also does not arise. The result of all this is that, in my judgment, the defendants have shown no arguable defence to the claim against them and there must be judgment for the full sums against each of them.

55. Had I been considering the question of conditional leave, on the basis that the defences raised were improbable, both in relation to the claim under the ESUAs and the guarantees, I would have demanded that, as a condition of leave to defend, the full sums should be paid into court. Mr Hacker

indicated that there were agreements by which the bank was already being secured by charges over assets et cetera. He also hinted at the defendants' impecuniosity.

As to the assets, it is significant that he is accepting and asserting that those agreements are binding despite the fact that they seek to secure the indebtedness which he says does not exist. But, in any event, the security is over property and assets located in Bangladesh and enforceable, presumably, only in that country. The defendants have offered no undertaking to consent to the enforcement of the security or to facilitate their enforcement in Bangladesh.

I cannot, on the material before me, say whether or not the security has any, and if so, what value. As to the impecuniosity point, no evidence has been filed to deal with the assets of the defendants and, in the absence of any, I certainly would not be prepared to infer that they could not raise the money they would be required to produce as a condition of obtaining leave to defend, had the question of conditional leave arisen, which it has not.

Accordingly, for the reasons I have attempted to give, I give judgment for the claimants on their claim.