HIDDEN TRAPS IN SHARI’AH DECISION MAKING
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The emergence of Islamic finance has introduced a new discipline known as “Shariah advisory services” (SAC). SAC adds a unique value proposition of religious law in the area of commercial life, where secularism rules almost unquestioned throughout the rest of the world. This phenomenon has emerged as a regulatory requirement to ensure Islamicity of Islamic financial institutions (IFIs) by establishing an independent Shari’ah Board (SB). According to AAOIFI, “Shari’ah board is entrusted with the duty of directing, reviewing and supervising the activities of the IFIs to ensure that they comply with Shari’ah principles”.

The following diagram depicts the cycle of SB involvement in the business of an IFI.
The exercise of taqfiqul manat is in fact an important component of Shari’ah advisory services provided to IIRs by Shari’ah scholars, which simply can be termed as “Shari’ah decision making”. Scientific research proved that there are various psychological traps, which significantly influence decision making. This article highlights only those traps that potentially lead to debacles in Shari’ah decision making, namely (1) the framing trap, (2) the status-quo trap, (3) the anchoring trap and (4) the confirming-evidence trap, along with antidots tips.

THE FRAMING TRAP

The first logical move in taqfiqul manat is known in business management science as ‘framing the problem’. It is like a frame around a picture that separates it from the other objects in the room. In Shari’ah decision making, framing creates a mental border that encloses a particular aspect of a situation to outline the key elements of it for in depth understanding. A mental frame enables the Shari’ah scholars to navigate the complex nature of a financial product, so they can avoid solving the wrong problem or solving the right problem in the wrong way.

Since majority of SB members (Shari’ah advisors) come from Shari’ah background, they typically rely on the information presented to them by the management of an IFI (i.e. business and product development unit) as they normally do not possess practical exposure to analyse directly a complicated product. Therefore, the way a product is defined to them by the management actually shapes the potential Shari’ah solution that SB members select (of course with some exceptional Shari’ah minds who have developed throughout the years a phenomenal comprehension of financial markets).

A substantial amount of studies found that “framing” significantly impacts outcome of a decision. The framing effect is an example of cognitive bias, in which people react to a particular choice in different ways depending on how it is presented e.g. as a loss or a gain, positive or negative. Similarly, there are evidences suggesting that framing influences Shari’ah decision in Islamic finance industry depending on the manner in which a financial matter is presented before the SB.

A famous example of the framing trap could be a fatwa endorsing conventional insurance as attributed to a famous Egyptian Scholar Muhammad Abdulh. A French man explained to him that insurance is like a mudarabah contract where one party provides capital and the other manages the fund. Later, he asked Muhamad Abdulh about its Shari’ah status. Muhammad Abdulh considered it a Shari’ah-compliant product based on the information presented to him. This was in reality “mis-framing” of the product.

Another latest example in Islamic finance would be the case of Islamic total return swap proposed by a multinational bank in 2007 and was approved by some Shari’ah scholars. The proposed product was claimed to be a Shari’ah-compliant version of the conventional total return swap (TRS), which had been christened as the “wadi” (voluntary promise) - based total return swap. The objective was to use non-compliant assets and their performance to swap its returns into a so-called Shari’ah-compliant investment portfolio.

The product was presented to Shari’ah scholars in a way reflecting that the performance of non-Muslim fund is just used as a benchmark index for the Islamic investment fund, resembling the interest-based pricing mechanism (IBOR) in Islamic banking products. However, its legality was heavily criticised by other scholars on the ground that wa’d is used as a mere stratagem to halalize a prohibited income. The analogy (wadi) between the use of LIBOR for pricing and the use of the performance of non-Shari’ah-compliant assets for pricing is both inaccurate and misleading. This is why both are not used for pricing. LIBOR is used to indicate the return, while the other is used to deliver the return.

Shiek Yusuf AlQarjie categorized this Shari’ah decision as an unfortunate one (due to mis-framing). It is an unfortunate shortcoming on the part of the Shari’ah board in this transaction that it failed to consider the context of the offering. It is an even greater shortcoming when it fails to consider the consequences the product will have for the entire industry. When it is clear that a product cannot be offered in its own form or, in other words, when it cannot be offered directly, but must be offered by means of a stratagem that is basically a derivative like a swap, red warning flags should go up. In such situations, the Shari’ah Board must pay careful attention to the circumstances of the offering. If the circumstances can be found to justify such a product, then it may be possible to grant approval. It not, however, approval must be withheld. In the case of promised returns from a referenced basket of assets, the assets must be Shari’ah compliant in order for the returns to be Shari’ah compliant. It really cannot be otherwise.
The true spirit of Islamic investment. Nevertheless, instead of being a status quo (normal) model, it resorted back to tawarruq-based models.

On the other hand, it is also observed that if a product is approved by famous Shari'ah scholars, it becomes a challenge for junior scholars to question it or even suggest an alternative due to the well-endowed reputation of those who endorsed it. To some extent, the status quo may be considered as a viable alternative. However, adhering to it out of fear will limit Shari'ah advisory options, and ultimately will compromise effective decision making.

To overcome this challenge, all other options should be carefully analysed. Exaggerating the effort or cost involved in switching from the status quo should be avoided. As far as questioning the opinion of senior Shari'ah scholars is concerned, the rule of thumb in Islamic discourse is to examine validity, authenticity and suitability of the underlying Shari'ah justification in the light of Islamic jurisprudence. This principle is exemplified by the evolution of Islamic jurisprudence into different school of thoughts, proving how constructive criticism has been playing a productive role throughout Islamic civilization. An academic criticism shall not constitute by any means a discretion.

The anchoring trap

Anchoring in psychology refers to the common human tendency of giving disproportionate weight to the first information he or she receives. During decision making, an initial impression, estimate or idea thrives subsequent thoughts and judgments. An anchor that prevents the boats from moving away. For example, the initial price offered for a used car, it acts as a reference point for anchoring. Therefore, Imam Muhammad – a famous Muslim scholar – is notdriving market prices. Journal of Financial and Quantitative Analysis, 44(2), 369–390.


Status quo trap

Status quo trap is an emotional bias and a preference for the current state of affairs. Psychologically, human brain considers a prevailing practice as a reference point and perceives other alternatives that vary from that baseline as inferior, hence undesirable.

This trap affects decision making eloquently as it underpins that human leaning is oriented on a status quo. Therefore, whenever a new product is introduced into the market, every other alternative is compared with the status quo. In the case of Islamic finance, the status-quo influences Shari'ah decision making from two aspects: management and scholarship reputation. It has been observed that in the Islamic financial system, there is still–unfortunately–serves as a baseline for Islamic law and business practices. For example, in 2014, Bank Negara Malaysia introduced mudarabah, musharakah and wakalah based investment account policy to portray Malaysia introduced muḍarabah, musharakah and than sins of replicating conventional products. The market has enthusiastically welcomed this new model of Islamic financial instruments.

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Conclusion

Psychologists have identified a series of manipulative flaws handpicked into human thinking process, which we often fall to their charms due to some kind of reasoning error. Shari'ah decision is apparently not an exception. By analysing the above facts, it can be concluded that these traps together point towards the following conclusions. First, an unfortunate Shari'ah decision might be the result of the partial information received by Shari'ah scholars and their subsequent limited perspectives. Such a decision will not only undermine legitimacy of the underlying Shari'ah justification but also deviates from the multi-dimensional aspects of Islamic finance, the Shari'ah scholar should carefully analyse the evidences affirming that a mufti (scholar) shall not confine himself (in making a Shari'ah decision) to what is written in classical books without taking into consideration the practical contemporary circumstances. Otherwise, the harm of such a Shari'ah decision will be more than its benefits.

To circumvent confirming bias, a scholar should examine evidences with equal rigour avoiding the tendency to accept confirming evidence without examining evidence of other schools of thought. Moreover, the Shari'ah scholar should adopt an open minded the capability to think about the problem independently before consulting others in order to avoid becoming anchored by their ideas. He should be vigilant to avoid anchoring by advisors, consultants and others from whom he solicits information and counsel. He should share with them as little as possible about his own ideas, estimates, and tentative decisions as revealing too much may result in his preconceptions simply coming back to him.

The confirming evidence trap

Confirmation bias is the tendency to “search for, interpret, favour, and recall information that confirms one’s pre-existing beliefs or hypotheses.”16 Research shows that decision makers sometimes seek out information that supports their prevailing instinct or point of view, thus thwarting subsequent thoughts and judgments, like an anchor that prevents the boats from moving away.

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To avoid such incidences, Shari’ah scholar should not automatically accept the initial frame formulated by one of SB members or the management. Rather he should always try to reform the problem in various natural ways. Sheikhd Qal‘Uman narrated that a shahab should get a deep understanding of the concerned case before issuing a fatwa.

Sometimes the fatwa seeker–due to his limited knowledge of Shari’ah– cannot explain features that determine Shari’ah ruling (if the case required). In such scenarios, the scholar (mualal) shall try to obtain the relevant information by other means. This happens mostly in commercial related questions in which the fatwa seeker presents a case according to his understanding and ignores the important aspects (that impacts Shari’ah ruling). While in some instances, the fatwa seeker deliberately misrepresents (mis-frame the matter) to suit his own interest. Therefore, Imam Muhammad – a famous Muslim jurist – used to market to understand nature of the business and the prevailing commercial trends.

In Shari’ah decision making, a common anchor could be the first proposal presented either by the management or a member of the SB. For instance, when an IFI intends to replicate a conventional product, its Shari’ah–compliant structure (al-thaw’ al– alif) proposed during brain storming session may serve as an axis around which the subsequent discussion will revolve. This is the case for many more good examples, such as the tawarruq-based Islamic financial instruments.

Such a game-playing legalism not only undermines the true spirit of Islamic law (maqasid al-Shari’ah), but also deviates from the multi-dimensional aspects of Islamic finance at both macro and micro level. A famous Hanafi jurist Ibn Abidin rightly pointed out that a Shari’ah rulings in classical texts should be carefully analysed. Exaggerating the effort or cost involved in switching from the status quo should be avoided. As far as questioning the opinion of senior Shari’ah scholars is concerned, the rule of thumb in Islamic discourse is to examine validity, authenticity and suitability of the underlying Shari’ah justification in the light of Islamic jurisprudence. This principle is exemplified by the evolution of Islamic jurisprudence into different school of thoughts, proving how constructive criticism has been playing a productive role throughout Islamic civilization. An academic critic shall not constitute by any means a discretion.

In Shari’ah decision making, a common anchoring bias occurs when a scholar seeks juridical evidences in classical literature (al–juzyat al–fiqhiyyah) to validate his decision regarding a specific case. Bar al– nanah (sale of an asset with its subsequent repurchase on the same day) is a prominent example in Islamic financial product but even the said prices are still relatively higher than the actual market value of the car.

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Due to its anchoring effect, it paved the way for reverse financial engineering that led to stagnancy and lack of innovation in Islamic finance. A prominent Islamic economist Najahul–ainah demonstrated, through macroeconomic analysis that the harmful consequences of tawarruq are much greater than the benefits generally cited by its advocates.17 He further articulates:

The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments. The market has enthusiastically welcomed this new model of Islamic financial instruments.