Shariah rules and crypto disputes: UAE court judgment and official Fatwa invalidate cryptocurrency transaction

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Brief

"Bitcoin is a digital currency that does not meet the legal and Sharia criteria that make it a currency subject to the rulings of dealing with official legal currencies recognized internationally. It also lacks the Sharia controls that make it a commodity capable of being exchanged for other commodities."

In a dispute over OneCoin cryptocurrency, a UAE court (Ras Al-Khaimah Primary Court) ordered the invalidation and rescindment of a cryptocurrency sale contract on the basis that the cryptocurrency transacted (OneCoin) was not a recognized currency or commodity in violation of Shariah rules and the Civil Transactions Law.

Reference to Fatwa No. 89043

The Court referenced Fatwa No. 89043 issued by the General Authority for Islamic Affairs and Endowments in 2018 which addressed Bitcoin and cryptocurrencies in general. The Fatwa addressed the status of Bitcoin in that it did not possess the necessary specifications to make it a tradable currency, like the approved currencies that are traded worldwide. And that it also lacks the necessary legal requirements to be considered a commodity for exchange with other commodities. The following

is the Fatwa content quoted by the Court in its reasoning:

“Firstly, defining Bitcoin: Those who call Bitcoin a currency describe it as a virtual, intangible electronic currency with no physical existence. These currencies, with their varying types, methods of access, and acquisition, have been widespread and known for several years. Among the most famous are Ethereum, Dash, Ripple, Litecoin, and Ethereum Classic, all of which are digital currencies, each with its characteristics, features, and ways of processing and generation. The purpose of resorting to such currencies is that they are decentralized, allowing individuals to control them, providing them with a high degree of privacy and confidentiality, and they cannot be tracked because they do not rely on official institutions and intermediary financial entities like banks. As they are not linked to any financial institution, they have no real assets or balances, are not protected by any financial regulations or laws, and are not subject to any regulatory authority. This has been one of the reasons for their exposure to massive increases or sharp declines, and in addition to all this: the unawareness of who is behind the promotion of this virtual currency makes it susceptible to damage and loss of value in the face of any sudden changes. For this reason, no country in the world, including the United Arab Emirates, has recognized Bitcoin as legal tender.

Secondly, the Sharia criteria considered in currencies: In the previous paragraph, we provided a description that clarifies the reality of this currency in its current state. In this paragraph, we mention the most important Sharia requirement for considering anything as currency, which is: state adoption, meaning that it should be issued by the state. This is what the scholars express as minting or striking coins. This is explained as follows: The adoption of monetary currencies is considered a special function of the state in Sharia. The state alone has the right to issue coins,

according to the adopted laws and regulations. This is explicitly stated in the texts of scholars, whether for metallic money – like gold dinars or silver dirhams – which have intrinsic value and were prevalent in the past, or for credit currencies that rely on the power of the law and do not have intrinsic value, such as paper currencies, which have become prevalent worldwide.

In conclusion, Bitcoin is a digital currency that does not meet the legal and Sharia criteria that make it a currency subject to the rulings of dealing with official legal currencies recognized internationally. It also lacks the Sharia controls that make it a commodity capable of being exchanged for other commodities. Therefore, it is not permissible to deal with Bitcoin or other electronic currencies that do not meet the recognized Sharia and legal criteria, as dealing with them leads to unsound consequences, whether for the individuals involved, the financial markets, or the entire community, and whether we consider it cash or a commodity, the ruling encompasses both cases."

(United Arab Emirates – General Authority for Islamic Affairs and Endowments, Fatwa No. 89043 dated 30/1/2018)

Invalidity of a cryptocurrency contract

In its reasoning in Primary Court case no. 87/2020 (Ras Al-Khaimah), the Court applied the statutes, case law, and legislative commentary, that govern the validity of contracts under the Civil Transactions Law. The following are extracts from the respective judgment.

"According to the provisions of Articles 125, 129, and 141 of the Civil Transactions Law, a contract is the binding commitment issued by one of the parties by accepting the other party's offer and their mutual agreement in a way that establishes its effect on the subject matter and results in the obligation of each party to fulfill what is required of

them to the other party. For a contract to be concluded, both parties must agree on the essential elements of the obligation and on the other legitimate conditions that indicate their essentiality, and the subject matter of the contract must be something possible, specific, or determinable and permissible to deal with. (Federal Supreme Court – Civil and Commercial Judgments – Appeal No. 226 of the year 25 Judicial – Civil and Commercial Circuit – dated 2006-03-14 Technical Office 28 Part 1 Page 525)

Article 202 of the Civil Transactions Law stipulates the possibility of having a future thing as the subject matter for counterbalances if the uncertainty is eliminated. The explanatory memorandum clarified the meaning of uncertainty as the inability to deliver, based on the statements of Ibn Al-Qayyim, which can be summarized in that there is nothing in the Book of Allah or the Sunnah of His Messenger (peace be upon him) that indicates that a contract on something non-existent is not permissible, and to what is mentioned in the Sunnah of the prohibition of selling some non-existent things as in his saying (peace be upon him) "Do not sell what you do not have". The reason is not non-existence, but uncertainty due to the inability to deliver. (Emirate of Abu Dhabi – Court of Cassation – Civil and Commercial Judgments – Appeal No. 286 of the year 2014 Judicial – Commercial Circuit – dated 2014-06-03 Technical Office 8 Part 3 Page 942)

In accordance with Article 210 of the Civil Transactions Law, an invalid contract is one that is not legitimate in its essence and is described as having a defect in its pillar, subject matter, purpose, or the purpose imposed by law for its conclusion, and it has no effect and is not subject to ratification, and anyone with an interest may invoke its invalidity. The court may rule on it by itself, as the invalid contract has no legal existence, like a contract. (Federal Supreme Court – Civil and Commercial Judgments – Appeal No. 284 of the year 25 Judicial – Sharia – dated 2004-01-27

Technical Office 26 Part 1 Page 240)”

Court finding

The Court ultimately found that:

“The sale of the cryptocurrency is not real and therefore not valid for trading. It does not meet the necessary criteria to be considered a tradable currency, particularly the requirement of being recognized by the state. Moreover, it cannot be considered a tradable commodity due to its lack of essential conditions, such as its existence and eligibility for trading. It is something that has not been proven to have actual existence or real value, and its ownership cannot be transferred, its value cannot be determined, nor can it be traded in any legitimate form.

As a result, the sales contract lacks the necessary legal conditions that must be present in any contract, such as the subject matter of the contract being possible, specific, or identifiable, and permissible for trading. In the case of a sales contract, specifically, the item sold must exist, be specific or identifiable, and eligible for trading. Furthermore, the cryptocurrency lacks the legitimate conditions that make it suitable for trading, as it is neither a tradable currency nor a commodity that can be exchanged, given that the state has not recognized it as a currency. It is also tainted with uncertainty due to the inability to deliver it.

Consequently, the contract that forms the basis of the claim is flawed, and is considered illegitimate in its essence and description. It has no effect, and the court has the authority to rule its invalidity on its own, in accordance with Article 210 of the Civil Transactions Law.”

When are crypto transactions legal?

Notwithstanding the quotation of the Fatwa used by the Court,

the complete text of Fatwa No. 89043 ultimately concludes as follows:

“It should be noted that this ruling applies specifically to these currencies that are the subject of the question at this time and are still beyond the control of responsible authorities. However, if a decision is made to regulate and adopt them and place them under a supervisory umbrella by those authorities, so that they meet the criteria that make them a legal currency, used in transactions between countries, then the ruling on dealing with them would take the same ruling as dealing with officially recognized currencies.”

The Fatwa, which states that dealing with cryptocurrencies such as Bitcoin is not permissible unless they meet the Shariah and legal criteria and are regulated by responsible authorities, can be considered compliant with manifest the Dubai Financial Services Authority (DFSA)’s recognition of certain cryptocurrencies.

The DFSA is the independent regulatory authority responsible for overseeing and regulating financial and ancillary services conducted in or from the Dubai International Financial Centre (DIFC).

The DFSA recognizes financial services and activities involving Crypto Tokens in two ways: (1) if the Crypto Token is included in the initial list published by the DFSA (Bitcoin, Ethereum, and Litecoin), or (2) if an application for recognition of a specific Crypto Token is submitted and approved by the DFSA. As per the DFSA’s notice of November 2022, Bitcoin (BTC), Ethereum (ETH), and Litecoin (LTC) are recognized Crypto Tokens.

The jurisdiction of the DFSA is within the DIFC, which is a special economic zone within Dubai. As a result, the DFSA’s recognition of specific cryptocurrencies and its regulation of related financial services may be considered to only apply

within the DIFC. This creates potential risks and uncertainties for cryptocurrency transactions conducted in other Emirates or outside the DIFC in Dubai.

In another example on a Federal level, the Central Bank of the UAE took the position in December 2020 that it is presently "not recognizing crypto assets as legal tender in the UAE, such assets are not recognized by the Central Bank as a means of payment and can only be used as assets for investment with a potential high risk".

Takeaway

The Central Bank, the Securities and Commodities Authority, the Financial Services Regulatory Authority and the Abu Dhabi Global Market, the Dubai Financial Services Authority and the Dubai International Financial Centre, the Virtual Asset Regulatory Authority, and even prosecutive authorities via anti-money laundering regulations have identified and defined cryptocurrencies and virtual assets in one way or another.

Notwithstanding, if a transaction turns contentious, there is an onus (on whichever party) to evidence that the cryptocurrency (or virtual asset) subject of the transaction fulfills legal and – potentially – Sharia criteria.

The laws and provisions are essentially static, until they are tested before the courts, and their application becomes dynamic, granting clarity over their actual application.

If a cryptocurrency is not recognized by the overseeing UAE authorities, transactions involving such cryptocurrencies may be deemed invalid pursuant to Fatwa No. 89043 and the Civil Transactions Law.

And this would apply to consideration or perception of the disputed cryptocurrency as either currency or commodity.

It is essential for individuals and businesses to be aware of

the legal status of the cryptocurrencies they are dealing with in light of the position of the UAE courts and consider the potential risks before engaging in transactions involving unrecognized cryptocurrencies.

And in caution against giving in to the escapism of crypto craze without adequate due diligence:

“There is a wisdom that is woe; but there is a woe that is madness. And there is a Catskill eagle in some souls that can alike dive down into the blackest gorges, and soar out of them again and become invisible in the sunny spaces. And even if he forever flies within the gorge, that gorge is in the mountains; so that even in his lowest swoop the mountain eagle is still higher than other birds upon the plain, even though they soar.” (Herman Melville, Moby Dick)

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