

Extracted Statement from Expert Report by Abdulkader Thomas

Mr. Kalair's management of the relationship between UM, Central, and the homeowners, appears to have been conducted with a bona fide attempt to comply with generally accepted principles of Islamic Finance.

Mr. Kalair would have had a reasonable expectation that funds paid into UM by homeowners as part of the mudaraba's revenues were available for use by UM to pay reasonable expenses of the mudaraba project including legal fees and scholars' invoices.

The invoice for deferred payment remitted by MCC would appear to someone in Mr. Kalair's position as being legitimate and actionable.

Based on this understanding of a mudaraba operation and Central's letter of August 26, 2005, UM would logically believe that Central would behave as a silent partner as opposed to a secured lender.

Two important features of a mudaraba are the exposure of the financier to the risk of financial loss, and the nature of termination. Mudaraba documentation may be very simple or quite complex.

In other words, UM would treat payments as a pass-through to Central, net of expected or relevant mudaraba expenses and UM's profit share.

The features of the UM - Central relationship were documented in a business loan agreement, two commitment letters and two collateral agreements. The business loan and commitment letters align to a mudaraba.

In summary, AAOIFI Shariah Standard No 40 allows deduction of direct expenses and shared expenses, but not indirect expenses that is the responsibility of the Mudarib.

Since expenses are not specified, UM would interpret that the provision of Islamic mortgages would require fatwa and Shariah audit.

As a result, UM would likely believe that financing Shariah compliant residential mortgages would allow UM to use mudaraba funds to establish and maintain evidence of Shariah compliance.

This view would have been supported in UM's view by the treatment of expenses in the collateral agreements. In MMSA 06, expenses are covered in Article 8 Servicing & Administration of the Mortgages section 8.2(q) "The Assignor may deduct, at its option, expenses and fees authorized pursuant to the Agreement and ...". This follows an identical clause in Article 6.2(vii) MMSA 05. As the mudaraba did not, in UM's view, allow much option, the Shariah expenses, except for meeting fees, were deferred until Central forced the liquidation of the mudaraba.

Finally, UM would account for the home finance musharakas on their own internal balance sheet, tracking any pre-payments or lump sum payments from homeowners in settlement of their total obligation. As the mudarib in the relationship with Central, such payments form part of the mudaraba project assets and may be used to pay eligible expenses under the mudaraba.

Therefore, the first step in termination would have been an accounting of the financial position of UM, whether or not there were legitimate mudaraba expenses like the Shariah expenses, and then a determination of final profit or loss.

The final accounting, taking into account settlement of outstanding expenses, should have had two clear outcomes:

a. The status of payments to UM as mudarib/obligor/servicing administrator from the housing musharakas. All payments into UM as servicing administrator should have then shown customers as either up to date or in arrears. But, in all cases, settled through their last payment of any type including prepayments.

b. Once the cash was in from the housing musharakas, the mudaraba would allow UM to settle related expenses. As noted above, UM would have understood these to include the long unattended Shariah scholars. In this case, the mudaraba might have terminated with a loss to the rab al mal being Central.

AAOIFI does not contemplate that the rab al mal is a traditional creditor.

UM under the MMSA 06 and MMSA 07 appears only to have an obligation to process the current portion of any payment to Central. This appears to allow UM to hold on behalf of the mudaraba any prepayments or lump sum payments beyond the anticipated monthly servicing charge.

During the ordinary course of operations, UM appears to do no more or no less than was required under the various agreements.

Instead, Central forced UM into receivership. The implications of this unorthodox termination included:

- i. UM was unable to abide by its obligations to its SSB, which had long been unpaid.
- ii. UM was unable to assure customers that their contracts would continue to be treated in a manner compliant with Shariah.
- iii. This, in turn, would cause harm to both the reputations of UM and Omar Kalair both within and without the Islamic community.

Forcing UM into insolvency proceedings also contradicted the assertions of mudaraba made in Central's letter of August 26, 2005.

There are three layers of Shariah governance. The first is the role of a Shariah Board. This is akin to an independent committee of the Board of Directors.

However, as a manager, Mr. Kalair would have taken at face value any assertion of research by his SSB as managers at IFIs are reliant on their opinions. Mr. Kalair was not in a position to question or verify the involvement of Egyptian scholars with his SSB. Indeed, AAOIFI standards require the preservation of separation and independence of SSBs from the IFI. The IFI (ie: Mr. Kalair in this case) is reliant on representations of its SSB upon which it then must act to maintain Shariah compliance.

Therefore, the arrangement between UM and its scholars to defer payment until UM was financially sound is not peculiar.

Most scholars do not send invoices.

Given the concern that the board had performed a substantial amount of work from 2004 until 2011, the scholars would have been worried that they would never be compensated. Whether advised by counsel or as a prudent measure to have a claim on UM, they submitted their invoice.

CONCLUSION

UM relied on Central's August 26, 2005 letter to interpret the relationship as an operational mudaraba.

As a mudaraba, Central should have honored payments made to UM and embraced the operational loss or the mudaraba or otherwise challenged the expenses.

Market practice allows for the mudaraba, in this case prepayments and lump sum payments collected from homeowners under the musharakas were legitimately used to offset the accrued expenses of the mudaraba venture. This included payment of legal fees and the consultancy fees of the SSB.

The use of precious metals to effect SSB payment, while unusual and not in accordance with industry standard, is not prohibited in Sharia law and may be explicable in the context of a Canadian IFI making payments to international Egyptian scholars around the time of the Arab Spring.