

Financing SMEs in France, the quiet struggle of Muslim entrepreneurs



FRANCE

By Jamil Henni

While multinationals dominate the public and media sphere, SMEs represent the backbone of France's economy, accounting for more than 99% of businesses and 55% of private sector jobs according to The National Institute of Statistics and Economic Studies, INSEE, and OECD. Despite their impact, outstanding banking loans to SMEs represent only 20% of outstanding loans to businesses, with an average annual interest rate 0.6% higher than the latter between 2010 and 2022, according to the OECD. For Muslim entrepreneurs seeking alternatives to usurious financing, the challenge is even bigger as no solution has been democratized to date.

Since 2008, the development of Islamic finance in France has mainly focused on offering services to individuals or large multinationals, with very few initiatives emerging to serve SMEs. Tax guidelines have been published for Ijarah Muntahia Bil Tamleek and real estate Murabahah financing transactions, but these adjustments only benefit banking institutions with proper licenses and the few Islamic windows in France solely focus on retail clients. Professionals must therefore think outside the banking framework to look for business financing.

While private equity remains the most widely used solution, it struggles to convince entrepreneurs who want to raise funds without losing decision-making power over their operations. The issuance of private Sukuk has been possible and recognized in France since 2012, following clarifications by the tax authorities and the Financial Markets Authority. SMEs have the possibility of issuing private Sukuk, described as financial instruments backed by real assets, compliant with Shariah and treated as bonds for tax purposes.

Another way for entrepreneurs to raise funds without losing control is to adopt a Mudarabah structure. Limited partnerships, SCA (societe en commandite par actions) and SCS (societe en commandite simple), are legal



structures with two distinct categories of partners: general partners, who are jointly and severally liable for the company's debts and limited partners, whose liability is limited to the amount of their contributions. General partners are responsible for managing the company, while limited partners act as passive investors. This distinction between labor and capital corresponds to the concept of Mudarabah in Islamic finance.

Limited partnerships first appeared in France in the 19th century, originating from a medieval maritime contract known as Commenda in Italian. From the Latin Commendare, to entrust, the Commenda was a means of avoiding usury that emerged in the 11th century in the context of medieval trade, the Crusades and commercial expansion in the Mediterranean Sea. As Mudarabah had been in use for several centuries in the Muslim world, it is likely that the practice of Commenda was a western variation of it, inspired during the Emirate of Sicily from 831 to 1091. Abraham Udovitch has supported this theory in his book 'Partnership and Profit in Medieval Islam'.

The SCA is easily adaptable to large-scale projects and can enable Muslim

entrepreneurs to create flagships of French industry. It is also one of the few French legal structures that allows capital to be legally raised from the general public through IPOs, which is not the case for most commercial companies. This legal form offers a coherent bridge between the requirements of French law and the principles of participatory Islamic finance. However, setting up and managing an SCA can be complex and costly, and is not particularly suitable for short- or medium-term collaborations, for which other solutions exist.

The SEP (societe en participation) joint venture is a specific legal form in French law. Losses and profits are shared among the partners, and the duration of the SEP can be fixed or indefinite. It can be used to carry out a one-off operation, or to bring together entrepreneurs for a joint project. One of the significant advantages of the SEP is the confidentiality of the partnership, which will not be visible to third parties. The SEP is particularly suitable when several entrepreneurs wish to carry out a joint project. Another solution is to choose the popular and flexible SAS legal form and have a partnership agreement drawn up by a law firm in order to structure a Mudarabah. Several entrepreneurs have made this choice to finance their businesses. It might offer less legal security than the SCA but is much more accessible.

The French legal framework offers considerable flexibility for setting up structures and private arrangements that comply with Islamic finance. Contractual freedom is considered a founding principle of contract law, and a constitutional principle, including the freedom to define the content of agreements, and very often allowing commercial contracts to be adapted to Islamic principles. While solutions do exist, they are unfortunately not widely available and are often unknown to French Muslim entrepreneurs, highlighting the need for better education, professional training and communication. ☺

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