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Modern Application of Bai' al-Sarf (Currency Exchange) From Maqasid Al-Shari'ah Perspective: A Scoping Review

Mohammed Farid Ali al-Fijawi*

Abstract

Bai' al-sarf widely known as currency exchange is an important sale contract both in classical and contemporary world. This scoping review looks into the objectives behind the rulings set by the Shari'ah for this sale contract. These objectives are sorted out from the commentaries of the hadith and the deliberations of the jurists through textual analysis method. Some of the modern applications such as T+2 and Islamic Foreign Currency Exchange (FX) Swap structures are briefly juxtaposed against the objectives of bai' al-sarf we discovered. Objectives of Shari'ah rulings in spot exchange is to avoid falling into the sale of debt against debt (*al-kali bi al-kali*), prevention of payment delay by one of the counter parties, prevention of conflict between the counter parties, and last not least to avoid falling into exchange contracts that will induce *riba*.

Keywords: Bai' al-sarf, currency exchange, spot seizing (*al-taqabud fi al-majlis*), equal counter-values (*al-tamathul*), sad bab al-niza' (closing the door of conflict), *riba*.

Bai' al-Ṣarf is sale of currency in exchange for currency, whether both of the counter-values are the same or not, i.e. the sale of gold in exchange for gold or the sale of gold in exchange for silver and vice-versa.¹ The Hanafi jurist, Al-Kasani (d. 1191) defined *bai' al-ṣarf* as sale of currencies (*bai' al-athmān*).² The Malikis differentiate according to the nature of the counter-values. When counter-values are alike, they call it *al-Murātalāh* and when the counter-values are different, they refer to it as *al-ṣarf*.³

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¹ Wahbah al-Zuhayli, *al-Fiqh al-Islami wa adillatuhu*, vol. 5, p. 3659.

² Al-Kasani, *Badai' al-Sana'i' fi Tartib al-Sharai'*, vol. 4, p. 453.

³ Wahbah al-Zuhayli, *al-Fiqh al-Islami wa adillatuhu*, vol. 5, p. 3659.

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The foregoing definitions agree that this contract, instead of consisting of an exchange of a commodity for a currency, exchanges one unit of currency for another. The Sharī’ah permits this type of sale provided that the exchange takes place on the spot, without the deferment of either one or both of the counter-values (*al-taqābuḍ fi al-majlis*), and provided that the counter values are equal when both are of the same genus (*al-tamāthul*).

The preceding conditions are supported by the following hadith reported by ‘Ubādah Ibn Şāmit in *Sahih Muslim*: “Gold in exchange for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, and salt for salt; like for like, and equal for equal, hand to hand. If the genus differs, then sell as you wish provided that the exchange is made hand to hand.”⁴ There are many other reports which vary in words but project the same meaning.⁵

The specific purpose of stipulating *bai’ al-sarf* contract with the condition of seizing both counter-values on the spot is to avoid *riba*. Umar Ibn Khattab said “do not to sell gold against gold while one counter value is absent and the other is present (*nājiz*) to the extent that if one party requests time to get the counter-value from his house, do not allow him. This is because in this I fear *riba* for you.”⁶ The Hanafī jurist, Burhān al-Dīn al-Mirghinānī (d. 1196) in elaboration of Umar Ibn al-Khattab’s report said that he did not allow payment of one counter-value in *bai’ al-sarf* without the other in order to prevent the contract from entering into the sale of debt against debt (*al-kali bi al-kali*).

Another purpose of spot seizing explained by al-Mirghinani is to establish equivalence between the degrees of the two counter-values. In sales where commodity is against money, the degree of money is higher than the degree of the commodity. That is why getting hold of the money is necessary before the seller can release his commodity. In *Bai’ al-sarf* since both counter-values are monies, the degree of both counter values are same. This requires both parties to exchange their counter-values on

⁴ Ibid. This hadith is reported by Imam Muslim (no. 1569), see Jamal al-Din Abu Muhammad Al-Zayla’I, *Nasb al-Rayah Takhrij Ahadith al-Hidayah* (Beirut: Dar al-Kutub al-Ilmiyyah, 2002), vol. 4, p. 72.

⁵ A set of different transmissions in relation to the above hadith can be seen in: Badr al-Dīn al-‘Aynī, *Nukhb al-Afkār fī Tanqīh Mabāni al-Akhhbār fī Sharḥ Ma’ānī al-Āthār* (Qatar: Wazarat al-Awqaf wa al-Shu’un al-Islamiyyah, 2008), vol. 14, pp. 270—277.

⁶ *Nasb al-Rayah Takhrij Ahadith al-Hidayah*, vol. 4, 109.

the spot in order to maintain equivalence between the two.⁷ None of the parties can be forced to pay first. If one is forced to pay first, he is left open to risks such as denial or unexpected-delay of payment by the second party.⁸

Shah Wali Allah al-Dehlawi presented two purposes of stipulating spot seizing (*taqabud fi al-majlis*) as a condition within the contract session. One of the two purposes is the one which we just discussed in the previous paragraph. The other purpose is to prevent conflict and dispute (*sadd bāb al-nizā'*) within the two contracting parties. There are high chances of conflict if a party does not receive its exchange on time; this is because money is needed by everyone. Benefit of money is only feasible after spending and releasing its ownership. If one party pays his currency and does not receive his exchange on spot, there are high chances that the buyer will spend the currency and not pay its price. This will result in conflict. In order to avoid such conflict, the *Sharī'ah* stipulates spot exchange of the counter-values from both parties.⁹

The purpose of stipulating both counter-values to be equal when the *bai' al-sarf* is between the same currencies is again for the purpose of not inducing *riba*. 'Abd Allah Ibn Umar reported the sermon delivered by his father Umar Ibn al-Khattab: "O People! Do not buy/sell one Dinar in exchange of two Dinars, and do not sell/buy one Dirham in exchange of two Dirhams because in this I fear *riba* for you."¹⁰ Basing on this, US Dollars for instance if sold against US Dollars, both counter-values have to equal.

The general purpose of *bai' al-sarf* is to enable people to benefit from each other through trade and transactions. Through *bai' al-sarf*

⁷ Burhan al-Din Abu al-Hasan Ali Ibn Abi Bakr al-Mirhginani, al-Hidayah Sharh Bidayat al-Muhtadi (Karachi, Maktabah al-Bushra, 2nd edn., 2007), vol. 5, 254. Equivalence between the two counter-values means that specification of both is feasible (*muta'ayyin bi al-ta'yin*). Money cannot be specified. For instance when someone buys merchandise for RM50. The seller cannot ask the buyer to pay him the RM50 which is in his pocket only. The buyer can pay with any RM50 he desires. Commodity is in the contra. The buyer can specify a unit/piece which he wants to purchase. The seller cannot replace the unit/piece specified by the buyer without permission.

⁸ Ibid., vol. 5, 178—179. If one party is forced to pay first it will amount to giving preference to one of the two equivalents without any reason. This is known as *tarjih bila murajjih*.

⁹ Sa'id Ahmad Palan Puri, *Rahmatullahi al-Wasi'ah Sharh Hujjat Allahi al-Balighah* (UP India: Maktabah Hijaz Deoband, 2003), vol. 4, 556.

¹⁰ Badr al-Din al-'Ayni, *Nukhb al-Afkar fi Tanqih Mabani al-Akhbar fi Sharh Ma'ani al-Athar* (Qatar: Wazarat al-Awqaf wa al-Shu'un al-Islamiyyah, 2008), vol. 14, pp. 288.

traders buy and sell their products in currencies of respected offshore countries. Foreigners irrespective of whether they are tourists or businessmen when visit another country are able to change their money to local currencies in order to utilize it.

The general practice of the IFI’s show, that they have categorized the paper-currency under gold and silver (known as *thaman haqiqi* or *naqdain*). Hence, they apply the Shariah principles of *bai’ al-sarf* to the currency exchange contracts. The Shariah advisory councils and IFI’s need to reach to a consensus in order to decide whether the current currency exchange contracts are to be governed by the principles of *bai’ al-sarf* or by the principles of any other Islamic contract. Looking at the foresaid discussion on the definitions of *bai’ al-sarf* and its conditions, one can understand that it is a contract for exchanging entities which has intrinsic values (*thaman haqīqī*) such as gold and silver. If paper-currencies are categorized under entities which stem its worth not from the intrinsic value but from the status accorded by the society (*fals/thaman iştīlāhī*) then paper-currencies will be subjected to different set of principles rather than the principles of *bai’ al-sarf*.

Basing on the current market practice of IFI’s in relation to the currency exchange, the currency exchange contracts can be placed under the rubric of *bai’ al-sarf*. This comes under the maxim of *al-ma’ruf kal-mashrut* (what is accepted by custom is considered acceptable by Shari-ah). If that is the case, then one have to see whether the *maqasid* of *bai’ al-sarf* or the *maqasid* of its terms and conditions are realized in the current currency exchange practices or not. We have discussed earlier that the preliminary requisite of *bai’ al-sarf* is mutual spot seizing which means both parties have to exchange their price on the spot without delay. In the present market practice even though the exchange transaction is called “spot”, the payment is settled in two days after the transaction (T+2). Shariah Advisory Council, Central Bank of Malaysia (BNM) in their resolution permitted the delivery and settlement of a spot foreign exchange transaction based on T+2. The council based its resolution on “customary business practice”.¹¹ The current market practice due to different time zones and geographical locations, require at least two days from the date of transaction to deliver the exchange payment. Even though the exchange payment is delivered after, the seller is informed of

¹¹ Bank Negara Malaysia, *Shariah Resolutions in Islamic Finance*, Kuala Lumpur, 2nd edition, 2010, 138.

the rate and amount of the exchange contract through a confirmation slip. The exchange amount is based on the rate decided in the contract. It is not affected by the rate-fluctuation. Having the rate fixed in this manner abolishes possibility of conflict arising between the two parties. This shows that the T+2 fulfils the maqāsīd of spot seizing. Some scholars consider the payment order as a form of possession as can be seen in a *fatwa* of Kuwait Finance House in answer to an enquiry on T+2. The *fatwa* says: “Giving a non-postdated check and issuing a payment order or using the telephone is considered forms of possession....”¹² One can say that this is an *hīlah* for the purpose of easing the flow (*riwāj*) of the wealth which is one of the *maqṣad* of *hiḏ al-māl*. However, the local currency exchange counters does not have the same excuses we mentioned earlier for justifying T+2. Their currency exchange should be on spot basis where both the buyer and seller have to take possession of their money within the session. IFI’s should have a separate set of parameters for local money exchange counters.

In the contemporary global market individuals and companies entering trading contracts have to deal in different currencies. This means the risk of fluctuation in currency exchange rate is always there. For the *maqṣid* of minimizing the risk of loss because of fluctuating rates, and maintaining the market stability the contracting parties have to resort to hedging mechanism. The hedging mechanisms are means (*wasā’il*) to achieve the aforementioned maqāsīd. To realize these maqāsīd, IFI’s resort to Islamic Foreign Currency Exchange (FX) Swap structures. One of the common structures is based on *wa’d* (unilateral promise). In this structure basically there are two sets of currency exchanges (*bai’ al-sarf*). One takes place at the beginning. Then a promise is made to undertake another currency exchange on a specific future date basing on today’s rate in order to avoid exposure to any fluctuation in the future.¹³ It is obvious that without the hedging purpose, this structure merely involves with a deferred currency exchange contract. Deferred currency exchange-contract does not fulfill the principles of *bai’ al-sarf*. Mainly the principle of spot seizing. The latter contract also comes under the rubric of sale of debt against debt (*bay’ al-kāli bi al-kāli*). The SAC resolved this

¹²Isra, “T+2 Delivery in Foreign Exchange Transactions”, <http://www.isra.my/fatwas/topics/treasury/risk-management/currency-trading/item/611-t%202-delivery-in-foreign-exchange-transactions.html>.

¹³ Asyraf Wajdi Dusuki, Shariah Parameters on Islamic Foreign Exchange Swap as Hedging Mechanism in Islamic Finance, 12.

mechanism only for the purpose of hedging.¹⁴ According al-Qarafi (d. 684) closing means (*sadd al-dharai’*) is as important as opening the means (*fath al-dharai’*).¹⁵ This substantiates that IFIs should project a balanced-approach towards developing means especially when it comes to the means which are two-fold such as hedging. On one side the hedging leads to the maqasid mentioned above while on the other hand it can easily become a trick (unlawful-*hīlah*) to indulge into contracts involving *riba*. Mechanisms should be designed to determine the objectives of the hedging parties, so door to induce *riba* is not opened.

The recent gold and silver investment offered by Islamic Banks also comes under the rubric of *bai’ al-sarf* which means the SACs should come up with solid parameters basing on principles of *bai’ al-sarf*. Increasing number of enquiries made in regard to exchanging, buying, and selling of gold and silver and the fatwa-responses seen on websites and social media clearly show that IBF’s and IFI’s are yet to include *bai’ al-sarf* as a stand-alone contract like other Islamic contracts in their resolution charters.

Conclusion

We saw that currency exchange is the day to day transaction applied by both the individuals and financial institutions. The need for the individuals such as foreign tourists, market traders, etc. is catered by the money exchange shops in the city. As a matter of fact, the real *bai’ al-sarf* as discussed in the legal texts is practiced by these shops where individuals buy and sell their money for currencies they need. The financial institutions cater the needs of offshore business partners and companies. Recently financial institutions have also ventured into sale of Gold. They apply currency exchange contract in modes that where not practiced in the classical sense. This study saw that there is a need for stand-alone parameters of currency exchange for both the money exchange shops and the financial institutions by the Governing bodies such as SACs.

Discovery of objectives behind the Shari’ah rulings and the terms and conditions set by the jurists in the classical *bai’ al-sarf* is important to be taken into consideration. These objectives will play the role of yardstick for evaluating the modern applications of currency exchange.

¹⁴ Bank Negara Malaysia, *Shariah Resolutions in Islamic Finance* (Kuala Lumpur, 2nd edition, 2010), 138.

¹⁵ Shihab al-Din al-Qarafi, *Al-Furuq* (Beirut: Dar Alam al-Kutub, n.d.), vol. 2, p. 33.

The limitation of this scoping review is that it only looked briefly into the T+2 currency exchange contract and the FX Swap based on unilateral promise (wa'd). A thorough study is needed to explore other the modern applications of *bai' al-sarf* in light of this research design.

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