

# POSSESSION OF CURRENCY PRIOR TO SALE: A *FIQHĪ* AND PRACTICAL ANALYSIS OF SPOT FX-I IN MALAYSIA

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## I. INTRODUCTION

This research draws upon a study conducted in 2013 by the Specialist Risk Unit (SRU) of Bank Negara Malaysia (BNM) on the foreign currency (FX) trading practices adopted by Islamic financial institutions (IFIs) in Malaysia. The SRU studied the practice of FX spot trading of five IFIs. Assessment was made on the structure of the products, operational practices, legal documentation and Shari'ah governance processes. The study found a potential Shari'ah issue in the practice of FX spot trading in that the IFIs do not have in their possession sufficient currency at the time of selling the currency. Accordingly, this research attempts to get a better understanding of FX spot trading by IFIs in Malaysia and the associated Shari'ah issues that arise therefrom.

## II. RESEARCH OBJECTIVES

The specific research objectives are twofold:

- i. To study the operation and process of FX spot trading from theoretical and practical perspectives; and
- ii. To analyse the Shari'ah issues associated with the practice of IFIs not possessing sufficient currency at the time of selling the currency (on the deal date).

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### III. RESEARCH METHODOLOGY

In meeting these objectives, this research adopts the semi-structured interview method with the involvement of the Treasury and Shari'ah departments of seven local IFIs. Twenty-one individuals were interviewed in twelve sessions involving more than 20 hours of interviews. Through these interviews, information relating to the real practice of FX spot trading in these IFIs, and the potential issues and challenges in having sufficient currency at the point of selling were gathered. The information and data collected from these interviews were assessed and analysed using the classical texts on Islamic jurisprudence, the views of traditional Shari'ah scholars, and the standards and resolutions issued by international organisations such as the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) and the Organisation of Islamic Cooperation (OIC) Islamic Fiqh Academy. The initial findings of this research were presented in a workshop attended by representatives from the Treasury and Shari'ah departments of most of the IFIs in Malaysia. In this way, a general view on the arising issues relating to FX spot trading was gathered from the industry representatives.

### IV. SHARĪ'AH ISSUES PERTAINING TO POSSESSION OF CURRENCY PRIOR TO SALE

This research discusses four Shari'ah issues pertinent to possession of currency prior to sale that may arise in the current practice of IFIs. The first issue relates to *bay' al-ma'dūm* (بيع المعدوم) (selling something that does not exist) whereby the IFI sells a foreign currency that is not in its ownership and possession at the time of dealing. Selling something which does not exist is a form of *gharar* (الغرر) (uncertainty), and *gharar* has been prohibited by the Prophet (ﷺ).

The second issue concerns *bay' ma laysa 'inda al-insān* (بيع ما ليس عند الإنسان) (selling something that is not in one's possession) as the IFI does not have sufficient currency in its account at the point of sale. The Prophet (ﷺ) has prohibited this type of transaction in a *ḥadīth* which says, “لا تبع ما ليس عندك” — “Do not sell what is not in your possession.”

The third issue pertains to *al-taṣarruf qabl al-qabd* (التصرف قبل القبض) (effecting a transaction before taking possession). There are *hadīths* which prohibit reselling what one has purchased before one takes it into one's possession. In one, the Prophet (ﷺ) said, "فإذا اشتريت بيعاً فلا تبعه حتى تقبضه" — "If you make a purchasing deal, do not sell it until you take it into your possession." The IFI in its practice could be contravening this *hadīth* as it purchases a foreign currency from an interbank party, delivery of which will be at T+2, but the IFI will not wait until T+2 to sell the currency to its customer. Worst still, the IFI is actually selling the currency before purchasing and taking it into its possession.

The fourth issue relates to the 'hand-to-hand delivery' (*yadan bi yadin* يدًا بيد) requirement in a currency exchange transaction. In Sharī'ah, both the exchanged currencies must be delivered to each of the contracting parties in the contract session before they part from one another. If the IFI does not have the currency in its possession, the question is how it would be able to deliver the currency immediately in the contract session.

In discussing the above Sharī'ah issues, this study suggests that they could be divided into two different categories. The first concerns the ownership and possession of the currency during the execution of the exchange contract. The second concerns the delivery of the exchanged currencies in the contract session before the contracting parties part ways.

This study argues that the first three issues raised against the current practice of spot trading are not relevant in a currency exchange transaction. Under the concept of *al-ṣarf 'alā al-dhimmah* (الصرف على الذمة) (currency exchange by taking liability to pay), the existence, ownership, possession and physical identification of the currencies being exchanged are not required on any of the contracting parties at the time the currency exchange contract is executed. Hence, the parties are allowed to borrow or purchase the currency from a third party after the execution of the exchange contract so that they can deliver it to the counterparty. However, the currencies must still be delivered and received by both parties before they part from one another. This is the view of the majority of Sharī'ah jurists including the Ḥanafīs, Shāfi'īs and Ḥanbalīs. Furthermore, this study submits that in the context of *al-ṣarf 'alā al-dhimmah*, the IFI is actually not

selling any specific money from any account but rather bearing the liability to pay. Contractually, there is no interconnection between the IFI's transaction with the interbank party and the transaction between the IFI and its customer. Therefore, the money which is purchased from the interbank party is conceptually not the money that the IFI is selling to its customer.

On the last issue, i.e., the hand-to hand delivery requirement in a currency exchange, this study contends that given the nature of foreign currencies that are located in nostro accounts in different countries with different time zones, different infrastructure and facilities for settlement, it is impossible to deliver the exchanged currencies during the contracting session. This contention is supported by an overwhelming majority of Shari'ah scholars who view that the delay in the delivery of currencies in forex trading is inevitable. Hence, a relaxation from the original prohibition is justified. In short, a delay for the period that is considered as the market norm, i.e., T+2 is allowed.

## V. RESEARCH FINDINGS AND CONCLUSION

This research finds that none of the IFIs involved in this research have sufficient amounts of currencies at the time they sell the currencies to their counterparties. Based on this premise, it is presumed that there is a very high probability that all the other IFIs in this country share in the same practice. This research also finds that all the IFIs involved in this research share the same reasons and concerns for not having sufficient amount of currencies prior to selling. It is further found that the difficulties faced by the IFIs, should they be required to have sufficient amount of currencies prior to selling, are real and valid, hence justifying a relaxation of rules to some extent.

This study concludes that the current practice of the IFIs is supported by strong Shari'ah evidence. These are, firstly, the texts and the understanding of the classical scholars on currency exchange, particularly the concept of *al-ṣarf 'alā al-dhimmah* (currency exchange by taking liability to pay); secondly, the principle of *al-aṣl fī al-ashyā' al-ibāḥah* (permissibility is the starting rule for worldly matters); and thirdly, the application of the principles of hardship

like *al-mashaqqah tajlib al-taysir* (hardship begets facility), *al-hājah* (need), *umūm al-balwā* (widespread issues which are difficult to avoid), and *al-urf* (custom).

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