The 179th Meeting of the Shariah Advisory Council (SAC) of Bank Negara Malaysia

The SAC of Bank Negara Malaysia in its 179th meeting dated 22 August 2017 ruled on the following:

Determination of Contract Session and Delivery for Bai` al-Sarf in the Current Financial Operation

SAC Ruling

The SAC ruled that the contract session for bai` al-sarf refers to the period of time during which the contracting parties enter into a contract, commencing with an offer (ijab), followed by an acceptance (qabul) to exchange monies between each other, and ending by the disengagement of the contracting parties physically or constructively, or through the waiving of rights to revoke the contract (takhayun). The delivery of money in bai` al-sarf shall take place during the contract session.

The practice of the delivery of money in bai` al-sarf, for instance on day two after transaction date (T+2) is construed to have taken place after the contract session. However, this practice may be allowed due to established customary business practice (‘urf tijari) arising from operational constraints. In addition, the delivery of money beyond the contract session may also be allowed in the event of unexpected disruptions.

Background

- Bai` al-sarf refers to a contract of exchange of money for money. In Shariah, the delivery of money (the subject matter) in bai` al-sarf shall take place during the contract session.

- In this regard, it is necessary to clearly define the contract session for bai` al-sarf in the context of current banking operations and to ascertain whether the delivery of money at T+2 is considered to have taken place during or after the contract session.

- This is important to ensure that foreign exchange (forex) trading activities undertaken by Islamic financial institutions (IFIs) are in compliance with Shariah.

Shariah Issue

- What is the definition of contract session for bai` al-sarf in the context of current banking operation?

- Would the delivery of money at T+2 be deemed to have taken place during or after the contract session?

(Please refer to the illustration on the example of money exchange contract)

Illustration: Example of money exchange contract

1. Customer purchases RM4000 from IFI with the counter value/ consideration of USD1000

2. IFI receives the payment of USD1000 from the customer and subsequently delivers the RM4000 to the customer

The exchange of USD1000 and RM4000 between the customer and IFI respectively shall take place during the contract session
Key Highlights of the SAC Discussion

What is the basis for the requirement of delivery of subject matter in bai` al-sarf during the contract session?

- The requirement of delivery of subject matter in bai` al-sarf during the contract session is based on the following hadith of Prophet (PBUH):

> “Ubadah bin al-Samit reported Allah’s Messenger (PBUH) as saying: Gold is to be paid for by gold, silver by silver, wheat by wheat, barley by barley, dates by dates, and salt by salt, like for like and equal for equal, payment being made hand to hand. If these classes differ, then sell as you wish if payment is made hand to hand.”

- There is consensus among Muslim jurists that the term يدا بيد (hand to hand) in the above hadith means that the delivery of both subject matters in bai` al-sarf to the contracting parties shall take place during the contract session before the disengagement of contracting parties.

- The delivery of money after the contract session does not fulfil the requirement of spot delivery in bai` al-sarf and will give rise to riba nas`ah.

In what situations would the delivery of money in bai` al-sarf be made at T+2?

- The delivery of money at T+2 occurs in the inter-bank foreign exchange (forex) transactions in which contracting parties are not physically at the same place, but execute the bai` al-sarf contract through one of the following mediums:
  (a) Electronic Platform
  - The bai` al-sarf contract is concluded through an automated matching system where a dealer expresses an offer (ijab) of bid or ask price of a particular currency. The acceptance (qabul) from the other dealer in the market will be automatically matched with such offer.
  (b) Over-the-counter (via telephone or chatroom)
  - The bai` al-sarf contract is concluded between the contracting parties, directly or through a broker, using telephone or chatroom.

- The delivery of money at T+2 is an established customary practice (`urf tijari) for the execution of bai` al-sarf via electronic and online mediums, but not applicable for a physical medium such as money changer/bureau de change.

What are the opinions of Muslim jurists and contemporary scholars on the contract session?

- Contract session refers to a meeting (ijitim`) to execute the sale contract.

- The majority of Muslim jurists opine that the contract session ends with the physical dispersal (iftiraq) of contracting parties.

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1 Imam Muslim, Sahih Muslim, Dar Ihya` al-Turath al-`Arabi, Beirut, vol. 3, page 1211, hadith no. 1587.
Contemporary scholars offer several interpretations on the contract session, which include:

(a) The contract session refers to a situation where two contracting parties face each other to negotiate on a particular contract. It is specified as a duration of time that commences with an offer and ends with the conclusion of contract; dispersal of contracting parties; refusal of one of the contracting parties to proceed the contract; or the shift of attention to another matter which not related to the contract.\(^6\)

(b) The contract session refers to a situation in which the contracting parties execute a contract; or a situation in which the same topic of conversation that relates to the execution of contract takes place.\(^7\)

(c) For a contract executed by telephone, the contract session ends when the phone conversation between the contracting parties ends.\(^8\)

(d) For a contract executed by email, telegraph or fax, the contract session commences when the offer reaches the counter party (offeree) and ends when the counterparty rejects the offer or shifts attention to another matter without accepting the offer.\(^9\)

**What types of contract sessions exist in current practice?**

Contemporary scholars classify the contract session into two categories:\(^10\)

(a) Actual contract session: Both contracting parties are physically at the same place and time; and

(b) Constructive contract session: Both contracting parties are not at the same place but at the same session/time where the contract is concluded through modern technology.

**Basis of Ruling**

The definition of the contract session confined to the “same place” is less relevant to current banking practice since most \(\text{bai}’\ al-sarf\) transactions in the banking operations do not involve physical meetings but rather through online or electronic platform. Hence, the most important factor that needs to be focused on in defining the contract session in current banking practice is “time/session” during which the \(\text{bai}’\ al-sarf\) is concluded.

The ending of a contract session with the disengagement (\(\text{iftiraq}\)) of the contracting parties, physically of constructively; or by waiving the right to revoke the contract (\(\text{takhayur}\)) is in line with the opinion of majority scholars as highlighted in the deliberation above.

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\(^6\) Al-Zarqa’, Mustafa Ahmad, al-Madhal al-Fiqhi al-‘Am, Dar al-Qalam, Damsyik, vol. 1 page 432.


Implication of SAC Ruling

- This ruling is important to provide clarity to the IFIs with regard to the definition of contract session. Based on this ruling, the practice of the delivery of money in bai` al-sarf, for instance on day two after transaction date (T+2) is construed to have taken place beyond the contract session. However, such practice may be allowed due to established customary business practice (‘urf tijani) arising from operational constraints. In addition, the delivery of money after the contract session may also be allowed in the event of an unexpected disruption.

- If the delivery of money after the contract session is not due to established customary business practice arising from operational constraints or an unexpected disruption, such transaction will be considered as riba nasiah transaction.

- This ruling also serves as a refinement to the ruling of 168th the SAC meeting dated 28 June 2016 on the contract session for bai` al-sarf.

The effective date of this ruling is subject to the effective date of Policy Document on Bai` al-Sarf which is expected to be issued by end of 2017.