

## Critical evaluation of the compliance of online Islamic Forex trading with Islamic principles

**Abstract:**

This paper explores Web-based forex trading which is currently being promoted as a possible investment opportunity, especially for those of the Islamic faith who are prohibited from dealing in interest-based transactions. Islamic forex is promoted to them as a permissible trade in currency from which they can profit.

This paper evaluates the compliance of Islamic Forex trading with Islamic principles through the research question: *What is the role of Islamic jurisprudence rulings in promoting or prohibiting forex trading? How Islamic forex trading differs from conventional forex to meet the principles of 'Islamic' finance?* And finally, can international modern financial institutions operate without the use of such a tool?

**Keywords:**

**Islamic Forex, Islamic Finance, Online Forex, Shari'a-compliant Forex, Islamic Forex Trading**

**1. Introduction:**

'Islamic' finance is a topic that has gathered momentum following the rise of Islamist political groups to power during the Arab spring. However serious discussion about 'Islamic' finance started after the financial crisis of 2007-2008 when Islamic financiers bragged that the financial crisis had resulted from conventional financial products and pointed their fingers to greed, innovation and laxity of regulation (Mazumder et al., 2010). However Zerban et al. (2011) discussed that misuse of existing financial products as well as non-compliance with financial regulations had contributed much to the 2007-2008 financial crisis

'Islamic' finance researchers and bankers have claimed that it was the robustness of their products and system that had prevented them from slipping in the financial crisis vortex (Blackaby, 2008). One of the authors of this paper worked in the commodity market from 2007 up until late 2009 and was involved in international trading and banking systems which prompted this study of the similarities and/or differences between traditional products and new 'Islamic' products.

This paper addresses the question: *How different is 'Islamic' forex from traditional forex?* Are 'Islamic' products really new or are they just traditional products rebranded to enhance their brand equity (Yackout & ElSahn, 2011). Money is what banks trade in and so forex trading, which involves the buying and selling of money, is an appropriate product on which to focus. There has been an explosion of online advertisements about 'Islamic' forex on the internet - all claiming to be permissible (*halāl*) or permissible and securing high income for traders. However, forex is based on options and/or future contracts traded in international markets and involve interest which is not permissible, so it is difficult to see how forex products, Islamic or otherwise, can meet Islamic principles.

**1.1 What is Forex Trading?**

Forex involves trading options on currencies (Salcedo, 2006), A foreign currency exchange rate is a price that represents how much it costs to buy the currency of one country using the currency of another. Currency traders buy and sell currencies through forex transactions based on how they expect currency exchange rates to fluctuate. When the value of one currency rises relative to another, traders earn profit if they purchase the appreciating currency and suffer losses if they sell the appreciating currency. Other factors, e.g.: adverse economic conditions; political events; war, can also reduce a trader's profits even if the trader "picked" the right currencies to trade (SEC, 2011).

### 1.2 Forex and risk management:

Currency options are becoming increasingly popular and are one of the best ways to hedge against adverse movements in exchange rates (Salcedo, 2006), especially for people involved in international trading transactions involving multiple currencies, e.g. multi-national companies.

### 1.3. Forex and pursuit of high income and risk taking:

Salcedo (2006, p30) cited Dan O'Neil, principal at Xpresstrade, as saying: *"Our clients are increasingly embracing options, not only for speculative purposes but also as tools to manage risk, increase portfolio diversification, and enhance income. One of the things that attracts investors to options is the fact that for almost any market outlook, time horizon and risk appetite, there is an appropriate options strategy"*. Accordingly, some people with a high appetite for risk or in pursuit of quick ways of achieving high income can use forex as a medium to achieve their goals, although many forex traders consider forex as being closely related to aggressive speculation (Cofnas, 2003).

### 1.4 Forex , liquidity and interest rates:

Since forex is currency trading, it is the most liquid financial market in the world (McFarlin, 2011). The major factors controlling the rise and fall of currency prices are:

- 1- Interest;
- 2- Commodity prices;
- 3- Employment;
- 4- Economic growth and trade;
- 5- Geopolitical events/acts of God;

Of these factors, the two most important factors are interest and commodity prices. Interest rates are controlled by a country's central bank (McFarlin, 2011). Commodity prices are controlled by future options markets which set prices based on the virtual interaction of supply and demand over future contracts but do not reflect either the physical ownership of commodities or their actual demand. As will become clear in the next section of the paper, the two major factors which enable forex trading, i.e **riba** and **gharar**, are in direct breach of 'Islamic' principles.

### 1.5 What is Islamic Forex Trading?

Shari'a – Islamic - law, prohibits interest payments (forex-learning-site, 2013; dailyforex.com, 2013). However, *rollover interest*<sup>1</sup> is an integral part of forex trading: So the question on one Islamic forex website is: ***"How can a Muslim forex trader from Saudi Arabia or United Arab Emirates trade currencies without violating religious/Shari'a law? The answer is to find a forex broker willing to offer an 'Islamic' forex account with no overnight interest. Such swap-free accounts are usually offered only to Muslims in order to prevent widespread abuse. To substitute for the revenue from a missing swap, Islamic forex brokers charge a flat fee for this service"*** (forex-learning-site, 2013 online).

As explained by Islamic forex brokers: *"If you are Muslim respectful of religion, you want to trade currencies here is the solution that is **halāl**. Here is a list of the best forex brokers offering an Islamic trading account to Muslim customers. An Islamic account allows Muslim traders to open accounts without interest during the night, which is not prohibited by Islamic law Shari'a"* (topforexbrokersonline, 2013 online).

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<sup>1</sup> **Rollover Interest:** Rollover is the interest paid or earned for holding a position overnight. Each currency has an interest rate associated with it, and because forex is traded in pairs, every trade involves not only two different currencies, but also their two different interest rates. If the interest rate on the currency bought is higher than the interest rate on the currency sold, then rollover is earned (positive roll). If the interest rate on the currency bought is lower than the interest rate on the currency sold, then rollover will be paid (negative roll). Rollover can add a significant extra cost or profit to a currency trade (Murphy, 2009).

**Shari'a's** prohibition of interest also applies to any interest earned on forex trading. To address this issue and to make it possible for Muslims to trade forex according to Islamic law, many forex brokers have developed 'Islamic' forex accounts which offer interest-free forex trading (aka no **riba** forex) (dailyforex.com, 2013 online).

However, as discussed above, interest is an integral part of currency pricing as well as part of the commodity prices declared by international commodity markets according to the future option prices, so: ***How can 'Islamic' forex be different from traditional forex if they both adhere to the same price-driving factors?***

## 2. Literature review:

The introduction of 'Islamic' financial products across the world has been in response to the growing needs of a significant segment of the global marketplace, i.e. Muslims, many of whom have refused to use interest-based financial instruments (Elfakhani et al., 2007). Several studies have been conducted to examine awareness, preferences, or service quality of Islamic financial products (Yakout & ElSahn, 2011). Dusuki (2008) also reported that the stakeholders of Islamic banks in Malaysia viewed social and ethical goals as more important than the mechanics of the bank's operations. Consumers made their decisions based not on knowledge of the quality and value of the products and services offered, but simply on religious principles (Bley and Kuehn 2004). 'Islamic' online forex trading has been introduced as a jurisprudence-compliant form of trading and advertisements for 'Islamic' forex can be widely viewed over the internet on several social media networks, especially on ethnic Muslim sites (e.g. Facebook, Islamonline, elwatannews, twitter, etc.).

Most Islamic banks clearly promote the 'Islamic' nature of their products through the names of the products which effectively brand such products - customers consider that such products have higher brand equity derived from brand trust (Yackout & ElSahn, 2011). Thus examining the true nature of Islamic bank products and the basis on which they were developed and operated will reflect the Islamic credentials of these products. According to above definitions – there is another puzzling feature of the terms used by financiers for 'Islamic' financial products, i.e. the insistence on using traditional Arabic words (rather than words more commonly used in modern Arabic dialects) written in the Latin alphabet for non-Arabic speakers, which effectively brand the product endowing it with more appropriateness than it may deserve, like the widespread use today, are the following instruments: **mudaraba** (trust financing), **moshakara** (partnership financing), **murabaha** (cost plus financing), **ijara** (Leasing), **Istisna'a** (commission manufacturing) and **salam** (advance purchase)

which relevant ones related to forex trading will be explained later.

Distinguished as an Islamic jurisprudence-compliant financial system and instruments, 'Islamic' finance started in the 1970s in some Arab countries, e.g. Saudi Arabia and Bahrain (Elgammal, 2006). Though we could consider that the momentum gained by 'Islamic' finance was from the adoption in oil-rich Arab countries of Islamic jurisprudence-compliant financial practices and products (i.e. 'Islamic' finance) when Saudi investors established the Islamic Development Bank (IDB) in 1975 (Rowey et al., 2006). However, its roots go back further to the 1960s (Kahf, 2002) and the contemporary Islamic movements led in the late 1940s and 1950s by Hassan Elbanna<sup>2</sup> and Sayed Qutb<sup>3</sup> in Egypt and by Sayyid Abul Ala Maududi in India and Pakistan<sup>4</sup> (Chachi, 2005). The main rules and guidelines for 'Islamic' finance were derived from the holy Quran and sayings of Prophet

<sup>2</sup> **Hassan Ahmed Abdel Rahman Muhammed al-Banna** (14 October 1906 – 12 February 1949) was a school teacher and prayer leader, best known for founding the Muslim Brotherhood a controversial political Islamic group.

<sup>3</sup> **Sayyid Qutb** (9 October 1906 – 29 August 1966) was an Egyptian author, educator, Islamic theorist, poet, and the leading member of the Egyptian Muslim Brotherhood in the 1950s and 1960s. In 1966 he was convicted of plotting the assassination of Egyptian president Gamal Abdel Nasser and was executed by hanging.

<sup>4</sup> **Sayyid Abul Ala Maududi** (25 September 1903 – 22 September 1979), was a Islamic scholar , journalist, theologian, Muslim revivalist leader and political philosopher, and a 20th-century Islamist thinker in India, and later Pakistan. He was political figure in Pakistan and was the first recipient of the King Faisal International Award for his services in 1979. He was also the founder of Jamaat-e-Islami, the Islamic revivalist party.

Muhammad (PBUH) and his recorded acts (Sunna) forged in one transcript by Muslim scholars - jurisprudence/**Shari'a**. The guidelines have been extensively studied by financial and economic scholars worldwide who have concluded that the general principles can be summarized as follows (Gait & Worthington, 2007):

- (i) Prohibition of usury or excessive interest - **riba**;
- (ii) Full disclosure of information in any contract or exchange and removal of any asymmetrical information in a contract - **gharar**;
- (iii) Prohibition of financing and/or dealing in sinful/socially-irresponsible activities and commodities regarded as non-permitted (**haram**) under Islamic, such as gambling and the production of alcohol for consumption;
- (iv) Business risk-sharing between capital provider (financier) and capital user (entrepreneur) in profits and losses;
- (v) Materiality - a financial transaction needs to have a 'material finality', that is a direct or indirect link to a real economic transaction;
- (vi) Prohibition of exploitation of any party to the transaction and promotion of justice and fair trade.

To this list, Rowey et al. (2006) added that capital should have a positive social and ethical impact and investors should not just consider profit. The point of prohibition of taking interest in itself enforces risk-sharing in project financing. Therefore, Islamic financiers can derive their profit either from fees or fixed charges and in partnerships share both profit and loss. Rowey et al. (2006) defined

**gharar** more widely than selling items which you do not own, i.e. not only the full disclosure of contractual terms and conditions or full description of goods but also included **maysir** (gambling or speculation) which is also prohibited by Islamic jurisprudence.

### 3. Main Types Shari'a -Compliant Financial Instruments

In order to get a sense of how the methodologies of Islamic jurisprudence have assisted in the creation of Shari'a-compliant financial instruments, a short list of the most popular products is provided below. Islamic financial instruments must not violate **riba** or **gharar**, and must be approved by the Shari'a board of accepted scholars appointed by each bank or financial institution. Such approval requires that every effort is made to share risk and ownership of the assets financed, and to specify with the greatest amount of certainty the quantities, qualities and prices involved of the product.

According to the above the closest equivalent to online forex trading under is the forward sale (**salam**) as it represents a product that will be exchanged at a future date not a product where a person supplies capital for another to invest or trade in for a share of profit or what has been previously defined as (**mudaraba**) venture capital or trust financing - each of which will be considered in turn below

**3.1 Mudaraba** is a form of financing based on partnership, whereby the capital required for a project is provided to the borrower, who manages the investment, pays back the loan with a predetermined percentage of the profit to his 'partner.' The partner's share in the proceeds will be determined by how well the project fares and he is therefore a partner in the risk of the project, and has 'earned,' the return on his investment. All Islamic schools of jurisprudence agree that the preset ratio should be in proportion to the capital invested. An Islamic bank may be the financing partner, or the trustee of the funds of a lender, acting as middleman in the transaction, considered a three-way partnership. This form of trusteeship is different from that in the West, because it involves profit and risk sharing by all parties.

The United Arab Emirates Civil Code, Article 693 is explicit about the risk-sharing properties of the **mudaraba**: "A **mudaraba** is a contract whereby the person owning property puts in the capital, and the **mudarib** (the borrower) puts in effort or work, with a view to making a profit" (Netzer, 2004: p20). The pedigree of the **mudaraba** can be traced back to the time of the life of the Prophet himself

(PBUH), who was said to engage in this type of transaction when he funded his business using the capital of his first wife Khadija bint Khuwaylid (Netzer, 2004).

### 3.2 Forward Sales (*Salam*) and *Istisna'a* (*Commission manufacturing*):

As previously discussed there are three basic conditions for the validity of a sale. These are:

- The commodity being sold must exist;
- The seller should have acquired the ownership of that commodity and as such its possible risks;
- The commodity must be in the physical possession of the seller.

These conditions are imposed to avoid ambiguity that could arise due to differences in timing between actual payment and delivery of the contracted good.

There are two exceptions: *Istisna'a* and *Salam*. Exceptions are accorded on the grounds that some but not all the conditions have been fulfilled and thus they are free from *gharar*. As in both of these sales delivery of the subject matter is deferred to the future, these can be termed forward sales. Under *Shari'a*, commodity markets can exist for the future delivery of goods subject to the rules relating to *Istisna'a* and *Salam*. However, modern futures markets that deal in futures (options, derivatives, swaps, etc.) do not qualify under these rules.

*Salam* is an ancient form of forward contract wherein the price was paid in advance at the time of making the contract for prescribed goods to be delivered later. Two terms "*salam*" and "*salaf*" have been used interchangeably in Hadith<sup>5</sup> to describe the contract for future delivery of specified goods with up-front payment of the price. The parties stipulate a certain time for supply of goods of specified quantity and quality. This is contrary to *bai' mu'ajjal* (deferred sale), in which goods are delivered to the purchaser in advance and the agreed price is paid at a stipulated date in the future. The word *salaf* (or *taslif*), which literally means payment in advance, refers to a sale by advance payment, and was used by jurists of Hijaz (Islamic scholars from the Eastern part of Saudi Arabia). In contrast, jurists based in Baghdad, Iraq mainly used the term *salam* for forward sale transactions. As the commodity to be delivered in future against prompt payment becomes a debt on the part of the seller, the transaction is termed *salaf* (loan) and implies a loan without any benefit (Udovitch, 1970). Here we can see the difference in ruling between two groups of Islamic scholars based on the difference in culture and trade requirements.

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<sup>5</sup> Hadith: the recorded collections of the traditions, acts, sayings of the prophet Muhammed (PBUH) that, with accounts of his daily practice (the Sunna) constitute the major source of guidance for Muslims, apart from the Koran.

#### 4. Methodology:

Searching the internet three websites were used to identify listings of Islamic Forex sites which claimed to supply Islamic Forex services for their customers or Islamic accounts as they called it (See table 1).

Web Site / List Web Site	5 cheapest forex brokers with Islamic swap-free accounts <a href="http://www.forex-learning-site.com/blog/2008/5-cheapest-forex-brokers-with-islamic-swap-free-accounts/">http://www.forex-learning-site.com/blog/2008/5-cheapest-forex-brokers-with-islamic-swap-free-accounts/</a>	Best Islamic forex broker - 10 best forex broker for Islamic accounts <a href="http://topforexbrokersonline.blogspot.co.uk/search?q=islamic">http://topforexbrokersonline.blogspot.co.uk/search?q=islamic</a>	Islamic Forex <a href="http://www.dailyforex.com/islamic-forex">http://www.dailyforex.com/islamic-forex</a>	Chosen for Comparison
<b>InstaForex</b> <a href="https://www.instaforex.com/">https://www.instaforex.com/</a>				
<b>FXOpen</b> <a href="http://www.fxopen.com/">http://www.fxopen.com/</a>				
<b>eToro</b> <a href="http://pages.etoro.com/">http://pages.etoro.com/</a>				
<b>Finexo</b> <a href="http://www.referforex.com/">http://www.referforex.com/</a>				
<b>Easy Forex 2</b> <a href="http://www.easy-forex.com/eu/">http://www.easy-forex.com/eu/</a>				
<b>markets.com 4</b> <a href="https://www.markets.com/">https://www.markets.com/</a>				
<b>Hotforex 1</b> <a href="http://www.hotforex.com/">http://www.hotforex.com/</a>				
<b>XM</b> <a href="http://www.xm.com/">http://www.xm.com/</a>				
<b>Exness</b> <a href="https://www.exness.com/">https://www.exness.com/</a>				
<b>FXPrimus</b> <a href="http://www.fxprimus.com/">http://www.fxprimus.com/</a>				
<b>RoboForex</b> <a href="https://my.roborex.com/en/login/">https://my.roborex.com/en/login/</a>				
<b>OCTAFX</b> <a href="http://www.octafx.com/">http://www.octafx.com/</a>				
<b>Hymarkets</b> <a href="http://www.hymarkets.com/">http://www.hymarkets.com/</a>				
<b>Ava Trade</b> <a href="http://www.dailyforex.com/">http://www.dailyforex.com/</a>				
<b>UFXMarkets 3</b> <a href="http://www.dailyforex.com/">http://www.dailyforex.com/</a>				
<b>FXCC</b> <a href="http://www.dailyforex.com/">http://www.dailyforex.com/</a>				
<b>FXCM</b> <a href="http://www.dailyforex.com/">http://www.dailyforex.com/</a>				

Table 1: Listings of Islamic Forex Trading companies

Each of the trading sites selected for analysis was included on at least two of the lists. This resulted in the identification of four companies (see table 2):

Company Name	Country of Head Quarters	Abiding Laws and Regulations
InstaForex	Not Stated (However all company contract and customer service telephone numbers have an area code of 007 which refers to Kazakhstan)	Not Stated
eToro	Cyprus	Authorized and regulated by the Cyprus Securities Exchange Commission (CySEC) under license # 109/10.
Easy Forex	Cyprus	Authorized and regulated by the Cyprus Securities Exchange Commission (CySEC) under license # 079/07.
markets.com	Cyprus	Authorized and regulated by the Cyprus Securities Exchange Commission (CySEC) under license # 092/08.

Table 2: Selected forex companies for comparison

5. Content Analysis of web sites offering `Islamic` forex:

5.1 First: Instant Forex Trading (InstaForex <https://www.instaforex.com/index.php>)

Searching the website to open an Islamic account directs the user to the open live account page (instaforex.com, 2014 online) which displays the Insta Service Ltd. Public Offer Agreement which notes that to open an Islamic account (a swap-free one), a customer should accept the supplementary "Swap-Free Trading Account Use Agreement", which includes the additional terms and conditions for converting a conventional account into an Islamic account and explicitly states in article 3 (b): *"Fixed fee rate of 2% (5%) is an interest rate"* (instaforex.com, 2014 online).

This explicit statement of the use of the word interest violates a key principle of `Islamic` finance that prohibits the receipt or payment of interest or the involvement in any transaction involving interest.

5.2 Second: Etoro (<http://www.etoro.com/en/social-trading/islamic-account>)

In the terms and conditions for the Islamic account the following statement was found: *"all open trades will be automatically rolled over, which normally poses a problem for those following Islamic law, due to the possibly usurious interest charged for the rollover"*<sup>6</sup> (etoro.com, 2014 online). Again this explicit statement of the use of interest violates the main guiding principle of `Islamic` finance that prohibits the receipt or payment of interest or involvement in any transaction involving interest.

5.3 Third: Easy Forex (<http://www.easy-forex.com/eu>)

According to this company's web site they offer trading accounts which adhere to Islamic law (*Shari'a*). With Islamic trading accounts, when traders extend their day-trading deals to the next day, no rollover is charged. Accordingly, the maximum duration offered for day-trading deals is limited (usually one week but it can also be shorter or longer depending on the currency pair traded) which is a very ambiguous statement from the company about the charges it imposes. However a more direct statement was found as a risk warning describing forex and commodities as leveraged products that carry a substantial risk of loss up to your invested capital and may not be suitable for everyone and asking that interested investors ensure that they fully understand the risks involved and do not invest money they cannot afford to lose – in other words it is gambling. This type of statement, albeit ambiguous, undermines one of main pillars of `Islamic` finance guidance, i.e. the prohibition of speculation and ambiguity (synonymous to gambling).

<sup>6</sup> See footnote(1)

**5.4 Fourth: markets.com** (<https://www.markets.com/trading-accounts/login.html?role=anonymous&checksum=9e275b6a98a226f91166d119e627974b>)

According to the company's web site they offer Islamic accounts to Islamic customer upon request but no details were provided concerning the nature of their regulations, however a risk warning was offered that the items of trade are high-risk investments and that forex trading and Contracts for Differences (CFD's) are "**highly speculative**" and carry a high level of risk and may not be suitable for all investors (Markets.com, 2014 Online).

**5.5 After reviewing all four companies it is important to mention the following facts:**

- 1- None of the four companies is supervised by any Islamic body but each complies with the international rules and regulations governing normal exchange markets and those of their respective country of operations.
- 2- The profits derived from forex options are from spreads (the difference between the 'ask' and the 'bid' price of a currency pair) and the pricing of these options is ambiguous and depends solely on technical analysis of market trends and curves as well as macro-economic factors far beyond the control of the involved traders.
- 3- Forex trades do not substitute for the real physical exchange of any goods, commodities or currencies but all are the logical settlement of sell and buy options.
- 4- Based on point 2 & 3 trade in forex options, if taken as a source of income, is simply a substitute for gambling for money as there is no real need for currencies to be traded apart from the pure pursuit of profit.
- 5- Finally, the investment in forex options is a high risk and highly-speculative business, which breaches the guiding principles of 'Islamic' finance, i.e. not to be involved in speculative transactions.

**5.6 Jurisprudence rulings on forex trading:**

One of the websites (dailyforex.com) provides endorsements of the *halāl* nature of its products by jurisprudence scholars in response to questions from various stakeholders – potential investors and employees. However, some of these endorsements are contradictory and some demonstrate little understanding of the mechanisms which underpin forex trading. These will be summarized and discussed in the next section of the paper. Table 1 provides a translation of Arabic statements of the issues considered and ruled upon by the jurisprudence scholars.

Dailyforex.com (2014 Online), one of forex trading company listing websites, displays a link listing jurisprudence rulings (*fatwa*<sup>7</sup>) that claim that based on their consent, forex trading is acceptable and permissible according to the laws of Islam, which show 16 jurisprudence rulings relating to 'Islamic' forex (see Table 3). The next section will prove a summary of some of these rulings.

<sup>7</sup> **Fatwa:** Islamic legal pronouncement, issued by an expert in religious law, pertaining to a specific issue, usually at the request of an individual or judge to resolve an issue where Islamic jurisprudence, is unclear. Typically, such uncertainty arises as Muslim society works to address new issues (islamic supremecouncil.org, 2014 Online).

No	Resolution Title	Issuing Authority	Name of Scholar	Country	Date
1	Ruling on working in international foreign currency markets	Advisory opinion Supreme Council	N/A	Jerusalem , Palestine	12/6/2005
2	About cash transactions in the sale and purchase of currencies	Islam Online	Prof. Yussuf AlQardawi	N/A	12/10/2006
3	Dealing on margin through financial markets	Islam Online	Prof. Ali Mohyulddin Al-Qarra Daghi <sup>8</sup>	N/A	24/11/2004
4	Working in brokerage firms in international financial markets	Islam Today	N/A	N/A	26/03/2001
5	Ruling on currency trading	Islam Questions and Answers	N/A	N/A	26/03/2001
6	Ruling on forex trading with payment of fees on keeping transaction for the next day	Islam Questions and Answers	N/A	N/A	26/03/2001
7	Currency Trading	Al Muslim	Dr. Khaled ElMaged	N/A	1/4/2005
8	How “Beit Alithithmar” (Investment House <sup>9</sup> ) Avoided Margin	Islam Online	Prof. Ali Mohyulddin Al-Qarra Daghi	Qatar	15/06/2006
9	Trading in Currencies Market	Islam Today	Dr. Rashed Ben Ahmed Al Elewy	N/A	13/11/2005
10	Resolution of Islamic Jurisprudence Council on Foreign Currencies and Commodities Markets	Islamic Research Magazine	Committee of the Islamic Jurisprudence Council	affiliate of Islamic conference organization	10-1997
11	Issues in Stocks and currencies	Sayd El Fawaed (Benefits Hunt)	Sheikh Saied Ben Saad Alhamad	N/A	N/A
12	Ruling on Mudaraba in Currencies	Islam Today	Dr. Abdalah Ben Mohamed Elsaedy	N/A	21/04/2002
13	Dealing Currencies online	Sayd El Fawaed (Benefits Hunt)	Sheikh Saied Ben Saad Alhamad	N/A	
14	Online Currencies Exchange	Islam Online	Group of Rulers	N/A	13/12/2005
15	Mudaraba on margin in International Markets	Islam Online	Mekkah Islamic Jurisprudence Council	N/A	4/10/2006
16	Dealing with companies selling and buying currencies	Islam Questions and Answers	N/A	N/A	N/A

**Table 3: Details of number of rulings, issuers, origin and date** Source: <http://arab.dailyforex.com/Forex-Fatwa retrieved 20/03/2014>

<sup>8</sup> **Prof. Ali Mohyulddin Al-Qarra Daghi:** Investment House Shari ‘a supervisory board executive member (invhouse.com, 2014)

<sup>9</sup> **Investment House** : The Investment House is one of the investment banks in the *Gulf Cooperation Council* (GCC) – (Kingdom of Bahrain, Kuwait, Sultanate of Oman, Qatar, Kingdom of Saudi Arabia and United Arab Emirates). The Investment House was incorporated in 2001 as a private shareholding company under complete supervision of Qatar Central Bank. The Company undertakes all investment activities that are permitted by Qatar Central Bank covering Investment Banking, Asset Management, Private Equity and Structured Finance. The Company focuses on different economic sectors; including Financial Services, Real Estate and Construction, Manufacturing and the Services Sector. Investment House geographically covers Qatar and other GCC countries (invhouse.com, 2014 Online).

**Ruling (fatwa) number one** says trading in currencies is permissible as long as the transactions are interest (*riba*) free and the investor trading in currency is considered to be a venture capitalist (*mudaraba*).

**Ruling number two** by Professor AlQardawi<sup>10</sup> also says that forex trading is permissible subject to the immediate payment and receipt (*takabod*) in cash for traded currencies - both rulings neglect all the issues associated with forex trading, previously explained.

**Ruling number three and eight** though replied by to by the same person (Ali Mohyulddin Al-Qarra Daghi) who is a member of the Shari'a Supervisory Board in an investment bank in Qatar called Beit Aliththimar (Investment House). In **ruling no. three** he says forex trading is permissible subject to immediate payment and receipt of currencies, transactions being real not fake and interest-free. He also added that the bank entry registration is acceptable instead of the physical receipt. While in **ruling no. eight** where he is asked in a long and rambling 721 word question how the investment bank of which he is a member of its *Shari'a* board<sup>11</sup> avoids margin trading, his 169-word answer explains that forex trading is surrounded by economic dangers and controversial jurisprudence issues and that the jurisprudence rules are hard to comply and involve high levels of risk, but in and in the third point of his reply he states that Investment House tries to prevent interest (*riba*) in all transactions and concludes by saying that although he allows forex trading he does not recommend it and recommends direct beneficial investment without detailing what this might be.


**Ruling number ten** is a Resolution by the Islamic Jurisprudence Council on Foreign Currencies and Commodities Markets which details the pros and cons of international exchange markets and their incompliance with Islamic jurisprudence due to inability to achieve immediate payment and receipt; physical goods exchange; selling what you do not own and monopolistic practices by large investors and it ends with recommendation for the Islamic governments to regulate their exchange markets whether they are permissible or not to prevent economic damages.

**Rulings number 12 through 14** allow forex trading subject to symmetry (in case of same currency); interest free; the intermediate company to received fees for their mediation not interest for the transaction to be venture capital; immediate settlement of transactions for payment and receipt; and not to trade in poor Islamic countries currencies special ones with weak economic conditions.

As discussed above none of the rulings directly marked forex trading to be non-permissible but each allowed it subject to achievement of specific conditions to be met without going into the details of why forex trading is used or what are the mechanisms of future options trading and how can the different use of tool affect its permissibility or non-permissibility.

It is important to note that the website which published the jurisprudence rulings add line at the end of each scholar answer with the same font of answer saying below are links to companies (four companies links are offered) that offer Islamic accounts for beginners. This text looks like part of the scholar's answer as if he is endorsing these sites.

Due to the controversial nature of rulings it was important to shed more light to identify how different scholars viewed forex trading it was important to note the keywords used in their answers and number of times repeated whether concerning the permissibility of forex trading or issues related to forex trading.

<sup>10</sup> **Yussuf AlQardawi**  **Ji.II U....J-::** Born 9 September 1926 is an Egyptian Islamic Contemporary Islamic theologian scholar known for his diverse works and ruling. He is best known for his programme, al-Shari'a wa al-Hayāh ("Shari'a and Life"), broadcast on Al Jazeera. He is also well known for IslamOnline, a popular website he helped found in 1997 and for which he now serves as chief religious scholar. Al-Qaradawi has published more than 120 books, including The Lawful and the Prohibited in Islam and Islam: The Future Civilization. He has also received eight international prizes for his contributions to Islamic scholarship (qaradawi.net, 2014)

<sup>11</sup> **Shari'a Board:** The role of our Sharia board is to provide religious and moral opinion and validation for all financial and operational aspects, in strict compliance with Islamic code and standards.

5.7 Islamic financial terms and issues discussed in jurisprudence rulings:

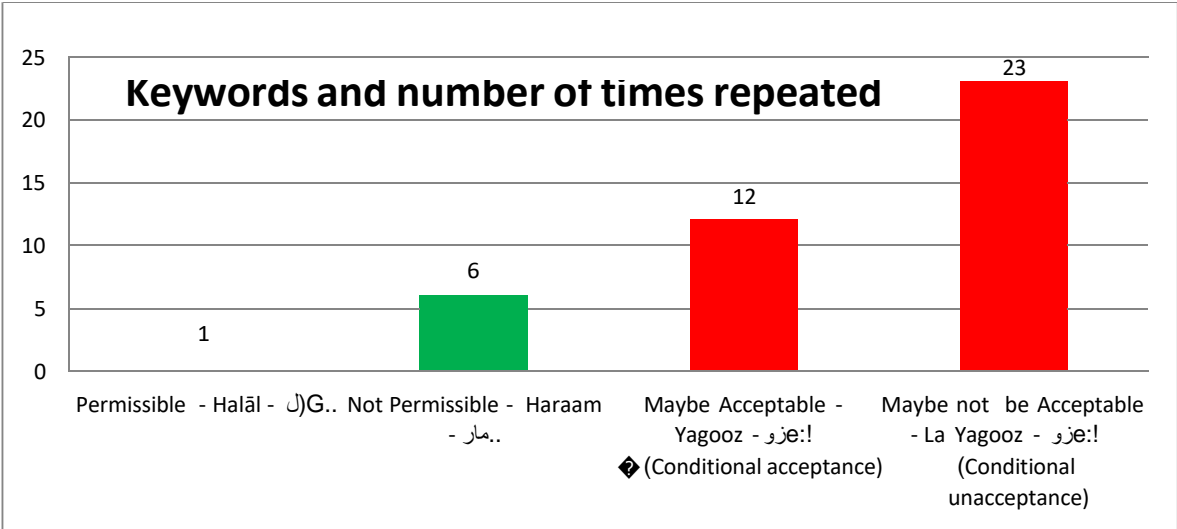


Figure 1: According to Islamic jurisprudence the scholars can either confirm the permissibility of an item or issue or its non-permissibility

Counting the number of times the words came up we can see skewedness in the scholars answers toward the non-permissibility of forex trading and their conditional disapproval of the trade which is shown in the second analysis of keywords issued and number of times repeated (Figure 2). Where most of the scholars are concerned mainly with loan and interest free transactions as the most two words repeated in their answers.

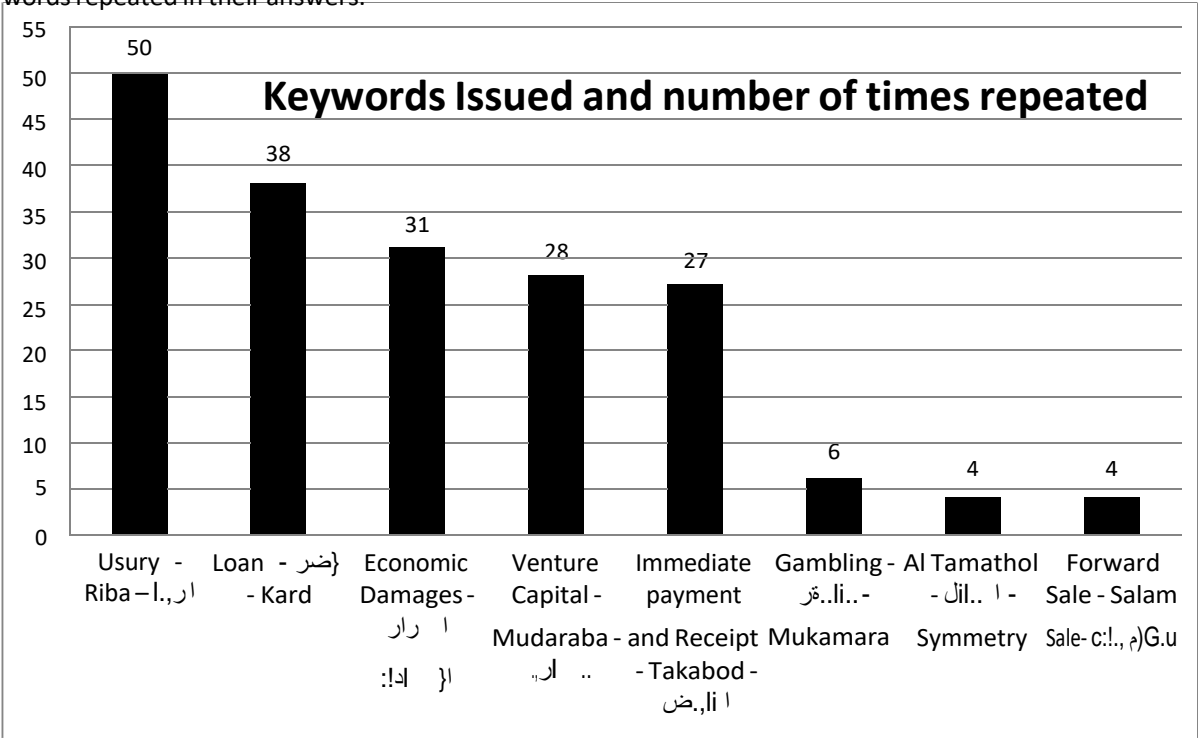


Figure 2: Identifies the keywords and number of times repeated in jurisprudence scholars' answers on the permissibility of forex trading

- **Usury – Riba - ربا:**

Avoid *riba* (USURY) any transaction involving payment of interest which could be considered as the trade mark of the 'Islamic' finance but even if the direct transaction does not include the payment or receipt of interest. However the term itself - '*riba*' in Islam, '*ribbit*' in Judaism and '*usury*' in Christianity - always refers to the illegal action or practice of lending money at unreasonably high rates of interest (oed.com, 2014 Online).

In macro-economics, interest rates are a key ingredient of any modern currency (e.g. REF).

Accordingly the ready-made frame of interest-free transactions need to be reviewed as the need to a modern definition of usury according to today's economic factors governing the issuance and management of currencies issued by central banks.

- **Loan – Kard - ائزض:**

The act of giving money, property or other material goods to another party in exchange for future repayment of the principal amount along with interest or other finance charges. A loan may be for a specific, one-time amount or can be available as open-ended credit up to a specified ceiling amount. Loans are forbidden in 'Islamic' finance due to their interest-bearing nature and their promotion of injustice due to people who own excess capital taking advantage of those in need of money and the issue of taking advantage of the someone's need cannot be separated from the term loan.

- **Economic Damage – 4 د.ا. رار!**

The issue of economic damage due to forex trading was discussed in several jurisprudence answers due in fear about the loss of wealth or the possibility of unleashing economic shocks as a result of unregulated and uncontrolled currency trading, especially in poor countries with weak economic conditions.

- **Venture capital – Mudaraba - 4 ر :**

Is a form of financing based on partnership, whereby the capital required for a project is provided to the borrower, who manages the investment and pays back the loan with a predetermined percentage of the profit to his 'partner'. The partner's share in the proceeds will be determined by how well the project fares and s/he is therefore a partner in the risk of the project, and has 'earned,' the return on his investment. All Islamic schools of jurisprudence agree that the preset ratio should be in proportion to the capital invested.

- **Immediate payment and receipt – Takabod - ائض :**

Takabod relates to the immediate payment and receipt within the same contractual session which can be defined in accounting as the cash basis versus the accrual basis. According to today's methods of payment and receipt accounting entries as well as bank correspondence are considered as actual confirmed irrevocable payments and receipts and the two-day delay on remittances are an international financial custom and the greatest scholars of Islamic jurisprudence and founders of the Hanafi, Maliki and Shafi'i Schools<sup>12</sup> accord the use of explicit customs (Udovitch, 1970). Therefore

<sup>12</sup> **Schools of jurisprudence:** These Schools were gradually consolidated or discarded so that there are currently four recognized Schools. The differences between these Schools of thought manifest in some practical and philosophical differences. Sunnis generally do not identify themselves with a particular School of thought, simply calling themselves "Sunnis," but the populations in certain regions will often - whether intentionally or unintentionally - follow the views of one School while respecting others. The Hanafi School was founded by Abu Hanifa an-Nu'man and is followed by Muslims in the Levant, Central Asia, Afghanistan, Pakistan, India, Bangladesh, Western Lower Egypt, Iraq, Turkey, the Balkans and most of Russia's Muslim community. There are movements within this School, such as Deobandis, and the Tablighi Jamaat, which are concentrated in South Asia and India. The Maliki School was founded by Malik ibn Anas and is followed by Muslims in North Africa, West Africa, the United Arab Emirates, Kuwait, in parts of Saudi Arabia and in Upper Egypt. The Murabitun World Movement follows this School as well. In the past, it was also followed in parts of Europe under Islamic rule, particularly Islamic Spain and the Emirate of Sicily. The Shafi'i School was founded by Muhammad ibn Idris ash-Shafi'i. It is followed by Muslims in Eastern Lower Egypt, Somalia, Jordan, Palestine, Saudi Arabia, Indonesia, Thailand, Singapore, Philippines, Yemen, Kurdistan, Kerala (Mappilas) and is officially followed by the governments of Brunei and Malaysia. The Hanbali school was founded by Ahmad ibn Hanbal. It is followed by Muslims in Qatar, most of Saudi Arabia and minority communities in Syria and Iraq. The majority of the Salafist movement, particularly in Egypt and Saudi Arabia claims to follow this School.

the insistence on the immediate payment of receipt in its physical form is not related to modern-day economics of financial transactions.

- **Symmetry – Tamathol** - ﺗﺎﻣﺎﺗﻮﻝ :  
According to Islam and the sayings of the prophet Muhammed (PBUH) we cannot sell one commodity for more of the same commodity – so, gold can be exchanged for gold and silver for silver of the same weight. In the days of Muhammed (PBUH) before modern paper currencies this would be ok. However, modern paper currencies that have no imbedded value or gold reserve cover (Fiat money<sup>13</sup>). Accordingly we should consider that gold and silver are commodities which hold value for their own not deriving value from other factors as per today’s currencies and the rule of thumb here is what we call today currencies is totally different from gold and silver coins circulated in ancient time not to mention different from currencies circulated up to the early 1970’s.

- **Gambling - Mukamar**- ﻣﻜﺎﻣﺎﺭ :  
Is the involvement in acts where the results are based on speculation or ambiguous (i.e. gambling-like activities), which make online forex trading ascurrently promoted form a source of quick and high profits, far from being a venture capital (*mudaraba*) or forward sale (*salam*) and falls directly as gambling as per definition of the gambling problem “Problem gambling is characterised by difficulties in limiting money and/or time spent on gambling which leads to adverse consequences for the gambler, others, or for the community” (Neal et al, 2005, pi). This coincides with the warnings found on almost all forex trading websites emphasising that they are high-risk investments, highly speculative, they carry a high level of risk and may not be suitable for all investors and that investors should not invest money they cannot afford to lose.

- **Forward Sale – Salam** – ﺳﺎﻟﺎﻡ :  
Difference between future sale as viewed by the Islamic Jurisprudence and what is actually taking place in the financial markets as future sales involves a physical good that will be exchanged on a future date but forex options have no physical existence and their offering and bidding is done on electronic platforms that settle the position of any customer logically and investors trading in international financial markets depends only on Contracts for Differences for making profits without any interest or need for the item of trade.

According to above issues discussed we can now determine breaches made to Islamic financial rules which constitute the cornerstone that all jurisprudence scholars have based their translations and rulings on.

General Islamic rules and how they are breached by such contracts:

Rule	Breach
(i) Prohibition of usury or excessive interest “RIBA”	According to the keywords analysis interest was at the top of the list of important issues not be breached and is considered a real taboo when it comes to `Islamic` finance however some scholars have expressed the view that the payment of administrative charges on loans are not interest and charges and so do not fall into the prohibition brackets. However, no clear-cut border has been drawn between what can be considered interest in money lending and what are administrative charges on the same except from change of name within the contract.
(ii) Full disclosure of information in any contract	The contract between the venture capital, investor or higher income

<sup>13</sup> **Fiat money:** money which derives its value from government regulation or law. It differs from commodity money, which is based on a good, often a precious metal such gold or silver, which has uses other than as a medium of exchange. Most modern paper currencies are fiat currencies, have no intrinsic value and are used solely as a means of payment. Historically, governments would mint coins out of a physical commodity such as gold or silver, or would print paper money that could be redeemed for a set amount of physical commodity. Fiat money is inconvertible and cannot be redeemed an issue which emerged in 1971, when the United States ceased to allow the conversion of the dollar into gold (Kaplan, 2003).

or exchange and removal of any asymmetrical information in a contract "Gharar"	seeker and the intermediary is a contract stipulating the use of the service of the financial intermediary to buy forex options in the international financial market either for a fee or for a share in profit as well as the use of the financial intermediary expert advice and none of this can be considered as non-permissible but no discussion on the option and on what basis it is bought and sold for profit
(iii) Prohibition in financing and/or dealing in sinful and socially irresponsible activities and commodities as regarded by Islamic religion such as gambling and the production of alcohol.	A number of jurisprudence scholars have criticized forex trading for irresponsible behaviour of traders solely pursuing profit and not caring for what this may cause to a country currency value or even the initiation of economic shocks, especially with poor countries suffering from fragile economic position.
(iv) Business risk-sharing between capital provider (Financer) and capital user (entrepreneur) in profits and losses;	There is no-risk sharing in forex trading the risk is borne by the trader who might lose all the amounts invested if adverse situations arise.
(v) Materiality, a financial transaction needs to have a 'material finality', that is a direct or indirect link to a real economic transaction;	There is no materiality or existence of physical goods in forex transactions as the forex options are contracts made on the international financial markets computer systems and settlement is made through the matching of bought and sold contracts
(vi) Prohibition of exploitation of any party to the transaction and promotion of justice and fair trade.	The pricing of forex options as well as the mechanism controlling the their prices are far from being clear or dependent on the supply and demand forces of the currencies

**Table 4: Islamic finance and breach made by forex trading**

Furthermore according to Rowley et al. (2006) the additional two rules stated in his research about the social impact of capital on society and ambiguity was not achieved by speculators trading in online forex and even the opposite can be summoned though currency value loss due to high speculation or irresponsible behaviour as well as the full mechanisms of option and future trading are ambiguous to most of the people even those who are involved in their trading to complex mathematical and nature.

Therefore what we currently need is a modern definition of **riba** (usury) according to modern-day conditions where monetary units in circulation do not represent value of their own but their own value are derived from other Macro economic factors totally out of the control of the people exchanging the currency and an understanding of the accounting recognition process that replace the physical payment and receipt in the early 19<sup>th</sup> century.

Also, there is a great difference between a forex trader who is using to option contracts or online forex trading to avoid losses due to the currency exchange price volatility and someone who is just pursuing profit out of online trading to satisfy his risk appetite (instead of gambling).

## 6. Conclusion:

The reliance on scholars' answers to determine whether forex is permissible or not has led to a very wide spectrum of jurisprudence rulings from the extreme rejection of the use of forex trading to the simple answer that it is permissible and this wide spectrum is either due to the simplicity of the question asked to the particular scholar or the deep understanding of the scholar of the Islamic religion jurisprudence who may have little knowledge about modern economic and financial management sciences and techniques (ruling number one as a prime example). On the other hand it seemed that more experienced scholars who combine financial understanding with knowledge of religion jurisprudence knew that it is impossible for financial institution to abide by the rigid rules laid by some jurisprudence scholars who depend on translations that are at least 60, if not hundreds of years old and looked for refuge in large grey areas where they can re-identify their trade.

Usage of forex trading is as Islamic as a kitchen knife which although very useful as a household utensil can be used as a weapon as up to 1,000 people a month are victims of knife crime in London, according to government statistics (Davenport, 2013), equally in the hand of an expert much more benefits can be drawn from compared to in the hand of an inexperienced or malevolent person. However it is important to point out that despite the hazardous nature of knives they have not been banned or outlawed as problems are always determined by who is holding the knife and his/her intentions; Similarly, the answer to the question of whether forex is permissible or not depends on how options and futures are used as risk management tools by people needing to avoid the risk of currency fluctuations and their adverse effects on their business not in people seeking pure income on excess cash on hand or in having a high-risk appetite.

Accordingly we can describe 'Islamic' forex in three ways - good, bad and the ugly.

**Good 'Islamic' forex** would be an important tool in risk management that no modern financial institution or trader could neglect or abandon and allow investments or trade to be exposed to currency volatility risk especially those in international trading transactions involving multiple currencies, e.g. multi-national companies operating in commodities market selling buying internationally and selling with local currencies.

**Bad 'Islamic' forex** would be the current version of Islamic texts translations issued by scholars disregarding modern financial and economic factors need to be updated to ensure that rulings are consistent with modern issues and above all to consider the difference between current currencies used as a valid tender between people and countries who hold no value of their own (like the ancient gold coins or even gold pegged currencies that use to exist) but derive their values from the strength of their issuers economies and policies set by issuing central banks who depend on interest as one of the tools to control currency value.

**Ugly 'Islamic' forex** is because some consider it as an income generator with no real knowledge of its use or behavior just depending on the online advertisement that it is permissible and high income provider without considering the negative effect such actions might have on their savings and country economy and never the less the permissibility of their actions according to Islamic religion jurisprudence though a careful reader would not miss the warnings in most rulings that irresponsible forex trading can cause economic chaos.

**As a final word** further research and probing with the banking industry employees in both the conventional and the Islamic banking sector is required to get a better understanding of: how financial products are created and managed; the role of bank rules and regulations in creating and managing different financial products. In addition it is important to find a modern-day definition of usury (*riba*).

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