

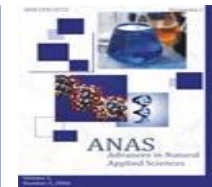


AENSI Journals

Advances in Natural and Applied Sciences

ISSN:1995-0772 EISSN: 1998-1090

Journal home page: www.aensiweb.com/anas/index.html



Wa^cd Principle in Structuring Islamic Hedging Products: Towards Realization of Maqasid Al-Shari^cah

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ARTICLE INFO

Article history:

Received 28 January 2014

Received in revised form 14

March 2014

Accepted 26 March 2013

Available online 10 April 2014

Key words:

Islamic hedging, FX forward, wacd, wacd, maqasid al-sharicah

ABSTRACT

Wa^cd or unilateral promise has been employed to structure innovative shariah compliant instruments to be used for hedging. Islam prohibits conventional forward currency contracts due to the element of *riba* and the violation of *bay^c al-sarf* rule. Since forward currency contracts are highly needed to hedge against exchange rate volatility, these contracts have to be structured carefully so as not to contradict with shariah principles. The usage of wa^cd has grown rapidly in recent years to replicate conventional derivative products in a shariah compliant manner. Although wa^cd is viable in practitioners' perspective, but from customers perspective, it fails to protect the right of customers since the wa^cd is not binding on the bank. Thus, wa^cdan or two separate unilateral promises which bind both parties offers an alternative since it can protect the right of both parties and hence can attain maqasid al-shari^cah. The issue is, to what extent the principle of wa^cdan differs from a contract and would the use of wa^cdan raise shariah issues similar to the conventional use of forward currency contracts? Would the application of wa^cdan really achieve maqasid al-shari^cah better than the single use of wa^cd? This paper aims to prove that wa^cdan is dissimilar to contract and to explore the application of wa^cdan in the light of maqasid al-shari^cah. To achieve the objective, this paper, which is qualitative in nature, utilizes content analysis method through deep and intense reading of classical and contemporary fiqh books and compares it with the current application in Islamic financial industry. To get the real view on the application of wa^cd in hedging products, interview with some shariah scholars and industry players were conducted. This paper concludes that the usage of wa^cdan in Islamic hedging products not only can preserve the wealth of people, but they could also achieve maqasid al-shari^cah since they could protect the right of all contracting parties.

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To Cite This Article: Azlin Alisa Ahmad and 2Mustafa 'Afifi bin Ab Halim., *Wacd Principle in Structuring Islamic Hedging Products: Towards Realization of Maqasid Al-Sharicah. Adv. in Nat. Appl. Sci., 8(3): 136-145, 2014*

INTRODUCTION

Islamic financial industry today is capable of providing complete banking solutions in fulfilling people's needs. For instance, the Islamic financial institutions in countries like Malaysia, Pakistan and the Middle East have successfully introduced and in some market segments replaced conventional home financing and conventional insurance with Islamic home financing and *takaful*. The industry has also introduced *sukuk* as an alternative to conventional bond. Despite the tremendous growth of Islamic product development, the industry still lacks the availability and an array of choices for hedging mechanism to mitigate risks faced by investors and people in business.

As Islamic finance grows, the need for Islamic hedging mechanism also grows due to the exposition of global risks especially currency risk and foreign exchange risks. Since the intensification of the globalisation process has resulted in greater volatility and uncertainty, hence there is a need for a global perspective in effectively managing these risks. In order to improve business confidence, a good hedging mechanism is highly needed to reduce the risks of currency exposure. The excessive use of derivatives instruments in recent years have in fact brought a lot of criticisms not only by academics and shariah scholars but also among practitioners themselves because they contribute to financial market instability and crises [6,14,15].

Islamic hedging products should not only have to be shariah compliant, but also must be competitive and attractive to the markets. Meaning that, under current circumstances, appropriate instruments to manage risks which are in compliance with shariah principles are still crucial. Competing side by side with conventional

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finance, and facing similar global economic and financial uncertainties and risks, the Islamic finance industry's search for Islamic solutions to meet changing market needs and lastly can attain *maqasid al-shari'ah*.

The conventional derivatives used in hedging such as FX forward contract is prohibited due to *riba al-nasi'ah* as it involves contract for future sale where both price and delivery are deferred. To ensure that FX forward is in line with *shariah*, *wad* is adopted in the first transaction, then followed by a real contract, that will be executed during the exchange of currency at maturity. Nowadays, many of the world's first *shariah* compliant derivatives such as Islamic cross currency swaps and Islamic profit rate swaps have been developed by Malaysian banks using *wad* principle. It shows that the practices of *wad* has become widespread since almost all the contracts offered by Islamic banks in Malaysia adopt *wad* principles to facilitate their operations.

Even though the usage of *wad* is comply with *shariah* principle, but it does not gives a perfect hedge to the customers. It fails to protect the right of customers in the event of default since *wad* does not binds bank on completing the transaction. On the other hand, *wad* is binding only on the promisor which is commonly on the customers. Thus, from customers perspective, *wad* fails to establish justice upon the contracting parties. As an alternative, the potentiality of *wadan* which binds both parties should be thoroughly scrutinized, so that Islamic hedging products do not only preserve wealth, but also the element of justice in the transaction towards achieving *maqasid al-shari'ah* is more important to be preserved.

Research Methods:

This paper is qualitative in nature and does not includes empirical data. The method used in this paper is document analysis and field research. To attain the objective of this research, content analysis method is utilized through deep and intense reading of classical and contemporary *fiqh* books. This method is also important in order to gather the relevant information related to the subject from various sources. Besides, to get the real view on the application of *wad* in Islamic hedging products, this study employs interview method. The interviews were conducted with the some *shariah* scholars and industry players. The industry payers consists of treasurers of some Malaysian Islamic banks, so that the current real picture of hedging products offered by Malaysian Islamic banks can be obtained. Meanwhile the interview with *shariah* scholars is important in order to get the *shariah* perspectives on which application of *wad* and *wadan* in hedging products.

Literature Review:

Wad means a promise that connotes an expression of willingness of a person to another group of people on a particular subject matter. The term *wad* which is also known as unilateral promise refers to a commitment made by one person to another to undertake a certain action or verbal disposal beneficial to the other party. Even though all Islamic jurists have unanimously agreed that promise is binding from religious perspective, but they have different views with regard to the legal status of promise. The fact is that, Malaysian Islamic banks applies the principle of unilateral binding *wad* which is binding only on the promisor. The unilateral nature of the *wad* makes it a very useful and flexible tool in structuring *shariah* compliant FX forward transactions.

The definition of *wadan*, on the other hand, cannot be found in any classical *fiqh* books. But, the term *wadan* is derived from the term *wad*, which is two separate *wad* done by two parties to do something in future. According to Aznan (2008), *wadan* refers to two unilateral promise whereby one *wad* is given by one party and the other party give the other *wad* independently. These to *wad* must be independent and not related to each other. Aznan and Shamsiah & Rusnah [42] mentioned that two main conditions that the double *wad* can be categorized as *wadan* are: (1) both two *wad* must not related to each other; (2) the effect of double *wad* must be different. The example of *wadan* that give different effect is: A gives *wad* to buy a computer when B willing to sell it. While B gives *wad* to sell a computer to A on a specified date in the future. Since the effect of *wadan* is different, so this kind of *wadan* is permissible. Nevertheless, *wadan* can also resulted in the same effect. For instance, A gives *wad* to sell a computer to B on 1 April 2011 if the price of computer is higher than market price. While B gives *wad* to A to buy a computer to A on 1 April 2011 if the price is lower that market price. On 1 April 2011, the same effect will occur, that is the contract of buying and selling is concluded.

Wadan, however, can also occurs in this situation. For instance, if A unilaterally promises to buy a computer X from B at future date T1 for a price P, and B unilaterally promises to sell computer X to A at a future date T2 for a price P, then the two promises together do not amount to a bilateral promise because they refer to different execution dates [7]. Aznan opined that there is no clear evident that allows the usage of *wadan* and so no clear evident that prohibits the usage of *wadan*. Based on that statement, this paper hence will explore the viability of *wadan* in Islamic hedging product, so that the *maqasid al-shari'ah* can be attained. In Malaysia, the usage of *wadan* in currency exchange transaction is not yet approved by all jurists because is may equitable to *muwa'adah* and the binding *muwa'adah* may be classified as a contract, so *riba* will occur.

Abu Ghuddah, on the other hand, differentiates between *wad* and *muwa'adah*. According to him, *muwa'adah* which is also known as bilateral promise refers to two reciprocal promises in which two parties agreed to do the same acts. A simple example for *muwa'adah* is, let say A promise to sell a car to B and B promise to buy the car from A. The resolution of Fiqh Academy of Jeddah decided that bilateral promise which

is binding on both parties are not allowed. With the definition of *muwa'adah*, AAOIFI ruled that binding *muwa'adah* on both parties is regarded as a contract. Thus, the Second Islamic Banking Conference held in Kuwait in March 1983 ruled that a bilateral promise in the sale of currencies by delayed payment is permissible in the bilateral promise is not binding. However, if the bilateral promise is binding, then the transaction is not lawful in the *shariah*.

According to Shariah Advisory Council (SAC) of Bank Negara Malaysia (2010), Islamic financial institutions are allowed to enter into a forward foreign currency transaction for hedging purposes based on *wadmulzim* which is binding on the promisor and the compensation for breaching of promise could be implemented. Nevertheless, no fee is allowed to be charged on the promisee because the upfront cash payment for forward currency transaction would lead to a bilateral *wad* which is not allowed by *shariah*. In Islam, the bilateral *wadis* not allowed to be used in forward currency exchange since it is akin to contract, thus *riba* will occur.

Even though *muwa'adah mulzimah* is claimed as similar to a contract, but Shamsiah & Rusnah [42] opined that *muwa'adah* should not be deemed as a contract but it is only a bilateral promise to execute an agreement on future date. Apart from that, all scholars agree that *wad* is different form contract because in the case of a contract, both of the contracting parties are obligated to complete the transaction and the delivery of the subject matter must be done. Al-Baz views that the permissible *muwa'adah* is the one that does not lead to a future contract that is based on future time (*al-bay' al-mudaf ila al-mustaqbal*), and the actual contract will be executed only when the real act of buying and selling occurs. The issue whether *muwa'adah* is binding or not is depend on the effect or the result *muwa'adah*. If the promisee had incurred some liabilities, then the fulfilment of *muwa'adah* is obligatory. The obligation is not due to it is considered contract, but the *muwa'adah* must be fulfilled to avoid harm (*darar*) to the promisee. If the promisor fails to fulfil it, then the actual damages must be paid because of the *darar*. But it should be noted that the binding nature of *muwa'adah* does not mean that it is a form of contract. Instead, the purpose of *muwa'adah* binding it to avoid harm to the other party [2].

Unlike Western law, Islamic law does not treat *wad* equal to contract. It is true that *wad* has to be binding, but the purpose of bindingness of *wad* is to avoid harm. In the contract of *murabahah*, for instance, if the *wad* is not enforceable in a court of law, they may make a *murabahah* as a risky contract if the client eventually refuses to take delivery of. Thus, the binding nature of *wad*, *wadan* and *muwa'adah* does not mean that they are equivalent to contract.

Based on an interview with Shamsiah [42], the reason why some scholars view that *muwa'adah mulzimah* is equivalent to contract is due to the same result arises from both of them. However, the claimed that *muwa'adah mulzimah* is equivalent to contract only based on the same effect arises is not right since contract has its own specific rulings and conditions. For instance, for the offer and acceptance, the following are required in a contract: (1) clear and understandable wording, conforming with the words and terms normally used in the custom of the parties to indicate a particular type of contract; (2) confirmation of *ijab* to *qabul*, which means that the meeting of the minds of contracting parties is essential; (3) connection of *qabul* (acceptance) to *ijab* (offer), which means that the offer is not withdrawn before acceptance [40]. On the other hand, offer and acceptance (*sighah*) in *muwa'adah* does not construct a valid contract since it only involves two reciprocal promises by two persons of their intent to enter into a contract in the future [22]. Meaning that, *sighah* in *muwa'adah* only involves a promise to do something in future, not to do something in present or in the past [2]. Since *sighah* on something in present or in the past do not refer to a contract, thus *muwa'adah* should not be claimed as similar to a contract.

Table 1 below illustrates the differences of *wad* and contract.

Table 1: Differences between *wad* and contract.

Aspect of differences	<i>Wad</i>	Contract
Offer and acceptance	In future, thus using the future expression	In present, thus using the present expression
Execution	Only a binding promise- the contract is not yet executed, thus no offer and acceptance.	The contract is executed- there is offer and acceptance upon the contract
Existence of subject matter	Subject matter is not necessary exist	Subject matter must be inexistence (except for some contract)
Delivery of subject matter	No delivery of subject matter	Delivery must take place.
Liability	Not a liability to pay the price yet	Liable to pay the price
Implication	No debt or other implications since the contract is not yet occur.	If the buyer does not pay the price yet, thus rulings on the debt will take place
Transfer of ownership	No transfer of ownership yet	Transfer of ownership is a must

The comparison above clearly proved that promise is not similar to contract. Thus, the views of *muwa'adah* binding on both parties is equivalent to contract due to *wad* gives a similar effect to contract is not a right opinion. The views that *wadan* may lead to a contract for future sale, whereby the exchange of currency is deferred to a future date is also false since *wadan* is only a mere promise, so it does not refer to a contract.

Therefore, it can be concluded that the usage of *wa'dan* in Islamic FX forward should not raise *shariah* issues similar to the conventional FX forward. In other word, the issue of *riba al-nasi'ah* will not arise in the Islamic FX forward based on *wa'dan* since the early stage in only a mere promise, not a contract.

Discussion on the Application of Wa'd In Islamic Hedging Product: Focusing of Islamic Fx Forward:

Hedging is an important risk management tool for a wide range of interested parties including fund managers, corporate treasurers, individual businesses, portfolio managers, pension fund managers, and bank managers. Any individual or institution having operations in currencies other than their local currency will face currency risk. Thus, forward contract is beneficial as a risk management tool since both parties have "locked-in" their price/cost, they would be in a much better position to plan their business activities. Thus, hedging not only provides the benefit of avoiding risk but the economic benefit of ensuring certainty and guaranteeing the future [22].

Without having a proper risk management mechanism and hedging tools, even when a company makes profit in its investment, but it actually makes a loss due to uncontrolled exposures to currency and exchange rate risk. Therefore, the activity of hedging is important to protect the wealth of people from losses and calamities. Furthermore, the need for hedging acknowledged in Islam. Islam recognises the concept of hedging and its importance particularly with respect to managing risk to protect wealth. One of the most important *maqasid al-shari'ah* is to preserve and protect wealth from being exposed to harm and damage or loss.

Wa'd is the most recent and viable concept to be applied in Islamic finance. Currently, this principle is widely used in Islamic capital market products as a tool for liquidity payment and hedging purposes. Although *wa'd* is still criticized from a conceptual perspective, in practice this instrument has become a contractual promise as it offers great flexibility. *Wa'd* can be used in Islamic FX forward to reduce or eliminate some unwanted risks such as price risk and exchange rate risk.

Generally, FX forward refers to an agreement to enter into the exchange of two currencies at a future date with the rates agreed upfront. This contract is important since an importer has the obligation to make payment at a future date in a foreign currency. Thus, the importer is exposed to risks that the foreign currency might appreciate, forcing him to pay more in domestic currency. Similarly an exporter who has receivables at a future date in a foreign currency have risks of losses if the foreign currency depreciates in future as he would receive less in export revenue in domestic currency.

Although FX forward transaction is important, but the all jurists have consistently asserted that the instruments and mechanisms used to manage risk must not in any way violate any *shariah* rulings. One famous *hadith* stated that: "Gold for gold, silver for silver, wheat for wheat, barley for barley, salt for salt, like for like, equal for equal and hand to hand" (Muslim, Kitab al-Musaqat, Bab al-sarf wa bay'al-dhahabi bi al-waraq naqdan). The *hadith* shows that currency which is categorized in *ribawi* items, the exchange must be in spot transaction, otherwise it will be constituted as *riba*.

According to Securities Commission, the exchange of currency must follow the principle of equal for equal and hand to hand in the case of homogenous currency and hand to hand in the case of different currencies to be exchanged. Both gold and silver according to the *hadith* represented the currency used as the medium of exchange during that particular time. In the modern era, gold and silver have been replaced by currencies. Hence, the requirement of *al-sarf* principles are extended to the exchange of gold and silver.

In other words, the above *hadith* have been regarded as providing the basis for the requirement that currency trading must be done on spot basis. The currency forward transactions contain the elements of *riba* since the parties involved wish to exchange currency sometime in future but the rate is fixed today. Therefore the contract is concluded today while the delivery of currency happen in future. Forward FX involves essentially two dissimilar *ribawi* (interest based) items, that is, two different currencies. The *shariah* position with regards to the exchange of two dissimilar *ribawi* items is that the exchange of two counter values must be on spot or simultaneous (hand to hand) (Hussain & Mehboob n.d).

It shows that forward contract is not permissible in Islam since it violates the principle of delivery with respect to exchange of currencies "hand to hand". Meaning that, both the importer and exporter really need to hedge against the volatility in foreign exchange risk, but since forward contracts of gold, silver or any monetary units are prohibited in Islam, they can hedge against risk using *wa'd* arrangement without involving the element of *riba*. Therefore, the importers can take foreign currency forward cover for genuine business activities on the basis of *wa'd* and simultaneously exchange of the currencies at the agreed time (Muhammad Ayub 2007). As Islam has ruled out the prohibition of entering into a foreign currency contract in which the concurrent possession of counter values by both parties do not take place, therefore, *wa'd* is viable principle to be adopted in the transaction.

Islamic FX forward based on *wa'd* refers to a unilateral contract involving two parties, where the first party promises with the latter party to buy or sell currency for settlement on a forward value date at the rate and amount agreed today. Only the party who makes the promise is obliged to honour the contract, but not the other party [22].

The figure1 below illustrates the structure of Islamic FX forward using *wa^cd* principle.



Fig. 1: Islamic FX Forward Based on *Wa^cd*.

Assumes that company A expected USD/MYR rates to strengthen and wanted protection by locking in the rate now and the bank would offer the FX Forward at 3.05. If company A accepts, then he and the bank are contracted to trade at that rate in 3 month's time. If the rate has strengthened further to 3.00, the exporter is protected as he can receive MYR6.1m (USD2.0m * 3.05) instead of MYR 6.0. The adaptation of *wa^cd* principle in the first stage of transaction makes the transaction of FX forward comply with *shariah* since on *wa^cd* date, the exchange of currency is not necessarily occur.

Thus, table 2 below depicts the differences and similarities of forward exchange contract and Islamic FX forward which is also known as Promisory forward exchange contract.

Table 2: Forward Exchange Contract and Promisory Forward Contract: A Comparison.

Forward Exchange Contract	Promisory Forward Exchange
1. Transaction between company A and bank is fulfilled at the dealing date (31/1/2010)	In the dealing date (30/1/2010), the company A only give <i>wa^cd</i> to do the transaction on 30/4/2010
2. Transaction fulfilled on the dealing date is binding and can be enforceable	<i>Wa^cd</i> on the dealing date is not binding and the parties can revoke the <i>wa^cd</i> for acceptable reasons
3. Currency rate is fixed on the dealing date (30/1/2010)	Currency rate is fixed on the dealing date (30/1/2010)
4. The delivery of asset is on the value date (30/4/2010)	The delivery of asset is on the value date (30/4/2010)

Source: Aznan (2009)

According to Syed Alwi, the mechanism of Islamic FX forward is as follows: Corporate customer can unilaterally make a promise (*wa^cd*) to purchase a currency, say USD for RM at a future date at a present fixed price. This is in the form of a promise to purchase made by a customer to a bank and the bank will provide an acknowledgement. Then, at maturity, the customer can make an offer to purchase the currency, for instance, USD for RM on a spot basis at the pre-agreed rate. Thereafter, bank accepts customer's offer and the currencies are exchanged.

As the transaction is made on a "spot" basis this fulfils the *shariah* requirement that currency trading is to be done on spot, the "promise element" only contains the promise to purchase and also the rate of exchange i.e. the price. Since *wa^cd mulzim* from only one party is not deemed under Islamic law as a contract, hence this can facilitate Islamic FX [30].

The illustration on how does *wa^cd* provide risk management is shown in the figure 2 below:

Based on the illustration above, it shows that Islamic FX forward transaction using the principle of *wa^cd* is able to provide risk management since the exporter is protected against volatility in exchange rate. Among the benefits of using *wa^cd* in Islamic FX forward are: (1) it is easy to use; (2) it is straightforward; (3) does not require complicated transaction; (4) the costs are the same as conventional; (5) easy to understand and implement [31]. According to Dar (2010), the interesting characteristics of promise which is considered as quasi-contract in Islamic law makes it ideal underlying agreement for structuring Islamic derivatives contracts for hedging purposes.

However, the drawbacks of *wa^cd* are the obligation is only on one party (problem if rate is in bank's favour and it choose not to exercise the *wa^cd*) and *wa^cd* concept is still not acceptable to all scholars [20]. Hence, the usage of *wa^cd* in Islamic FX forward fails to provide a complete hedge as demanded by the market players in Islamic financial industry [9].

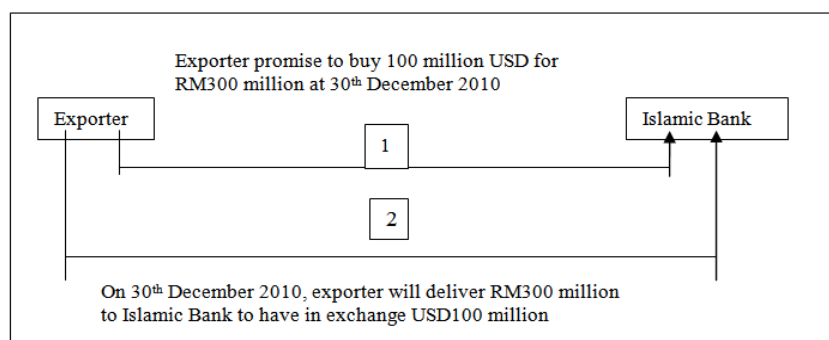


Fig. 2: Islamic FX Forward Using *wa'd*.

Source: Mohd Daud [30]

In the current practice of FX forward, delivery and settlement of transactions of foreign currency are not made in cash at a time and date when a contract is entered into. For transactions in the spot, submission and settlement will only be made on T+2 (two days after the date of the transaction), while that of transactions in futures (forward contract), settlement will be made on the date such forward one month, three month or so on a contractual basis (Bank Negara Malaysia 2010). The application of *wa'd* can be considered as new in Malaysia, especially in the Islamic hedging products. Thus, the fact is that, yet, there is no default in promise that need to be dragged to the court of law.

Findings: Maqasid AL-Shari'ah Perspective on the Usage of WA^CDAN:

The ultimate goal of *shariah* is to improve and protect the well-being of mankind. Since of the purpose of *shari'ah* is to protect the basic necessities of people, therefore the protection of wealth (*hifz al-mal*) is one of the essential values that need to be preserved. Preservation of wealth which is one of the *maqasid al-shari'ah* is considered in the five essentials values that need to be protected at all costs. Hedging which refers to a process of handling risk in an effective manner can help people in reducing some of unfavourable risks, hence protecting the wealth of people from losses or *darar*. Hedging also allows people to plan better, thus it reduces price fluctuations that will then lessen the costs.

In Islamic law, hedging with the aims to protect wealth is not only allowed, but it is very much encouraged as long as it is free from elements that are contradict with *shari'ah*. Without hedging that has an important role in preserving social well-being, it may lead to a destruction of wealth which is not permissible in Islam. Thus, it may be argued that failure to protect one's property in the face of risk and bankruptcy is tantamount to neglect of one's duty which is undesirable from the viewpoint of Islam. In addition, if one do not take any step to protect wealth from certain risks, it is considered violating the objectives of *shari'ah*.

Hedging is also positively related with *maqasid al-shari'ah* since it preserve the wealth of people by providing assurance that the objectives are more likely to be achieved, damaging things will not happen or are less likely to happen. Mitigation of the currency and exchange rate risk, for instance will help the growth of international Islamic financial instruments. Because of the preservation of wealth falls under the category of necessity, therefore hedging that allows the market participants at a micro-level to avoid undesirable risks can attain bigger *maslahah*.

As mentioned before, hedging gives protection to the investors from being exposed to the volatility of market fluctuations, thus it can preserve the wealth which is one of the *maqasid al-shari'ah*. Siddiqi (2009) opines that economic prosperity and the efficiency as well as stability of Islamic financial system depend on the prosperity and proper handling of risks. However, the lack of hedging products for managing risks has put many investors and institutions involved in Islamic finance at a disadvantage.

It should be noted that Islam meets the need of human in all aspect of life in terms of its flexibility and justice. Any ruling that replaces justice with injustice is a ruling that does not belongs to *shariah*. This is because *shariah* is universal which aims to serve the interest of mankind (Ibn Qayyim 1968). It is to establish a balance by way of fulfilling rights and obligations and by eliminating excess and disparity in all spheres of life. The concept of justice in *shariah* is not confined to the judicial aspects but it covers all areas of life including individual justice, social justice and international justice. Thus, the application *wa'dan* in Islamic hedging products must be structured in such a way that it can uphold justice to the parties. Both parties must feel protected and should be given full information and knowledge of the ultimate outcome of the contract. By protecting the right of both parties, then *maslahah* can be attained.

Kahf (2006) states that the role of Islamic financial engineering over the last four decades has been to develop contracts that fit this new industry and its success/failure can be accessed on the basis of the extent to which new contracts maintain the main characteristics implied by the prohibition of *riba* and preserve the objectives of this prohibition. Therefore, Asyraf Wajdi & Nurdianawati Irwani (2007) argue that one of the

biggest challenges of Islamic banking and finance industry today is to come up with products and services that is *shariah* compliant or legitimate from Islamic point of view without undermining the business aspects of being competitive, profitable and viable in the long run.

Since, the ultimate goal of *shariah* is to meet the public needs in good faith and protect them from harm, it is therefore important for Islamic financial industry to ensure that the development Islamic hedging products would give equal protection to all contracting parties. It is vital that counterparties have access to such products, in order for Islamic finance to continue to grow and an increased level of financial intermediation to occur as a result, with a deepening of the Islamic market. This can only be beneficial for finance as a whole.

In addition, it is important that both the essence and the object of the contract must satisfy all of the *shariah* requirements. According to Mohamad Akram (2010), most of the scholars nowadays give more attention to the “means” rather than “end”. In other words, priority is given to the form, not a substance. Therefore, in order to ensure that the innovation of products will be accepted globally and both the means and end are comply with *shariah*, the potentiality of *wa^cdan* must be scrutinized.

In the context of Islamic FX forward, the usage of *wa^cd* fails to give protection to both parties since there will be an open exposure, thus it does not give a perfect hedge (Engku Rabiah 2011). From customers’ perspective, there are some customers who are not favour to enter into Islamic FX Forward since the unilateral *wa^cd* is binding on the promisor only which is normally on the customer. To customers, Islamic bank being the promisee does not have any commitment to the FX transactions. In this issue, the unilateral *wa^cd* which fails to give equal protection to both parties. Even though banks will never default due to keep their reputation, but from customers’ perspective, it does not fair. Since the usage of unilateral *wa^cd* is not yet accepted totally, therefore, its usage must be replaced with the principle of *wa^cdan* that bind both parties.

Therefore, the viability of the usage *wa^cdan* in Islamic FX forward will be explored further. The structure of Islamic FX forward by adopting *wa^cdan* have to provide adequate protection to both parties in order to achieve *maqasid al-shari’ah*. According to al-Ghazali (1937): “*Maslahah is the protection of the objectives of shariah, which consists of five values: preservation of religion, of life, of intellect, of progeny and of wealth. What assures the protection of these five values is maslahah (public interest), and whatever leads to its lost is considered mafsadah (mischief) and its prevention and removal is maslahah*”.

Al-Ghazali (1937) further clarifies that: “*As for maslahah, it is essentially an expression for the possession of manfa’ah (benefit) or the removing of madarrah (harm), but that is not what we mean by it, because possession of benefit and removal of harm represent human goals, that is, the welfare of humans through the attainment of these goals. What we mean by maslahah, however, is the preservation of the ends of the shariah.*”

There are also some legal maxims showing the importance of choosing the lesser harm in order to attain *maslahah*. Among them are:

درء المفساد اولى من جلب المصالح فإذا تعارض مفسدة ومصلة قدم دفع المفسدة

Meaning:

Prevention of evil takes priority over the attraction of benefit. If there is contradiction between harm and benefit, thus prevention of harm is getting priority.

الضرر الأشد يزال بالضرر الأخف

Meaning:

A greater harm is eliminated by means of a lesser harm.

This maxim shows that Islam ask people to eliminate harm. Islam give choices for the two harm that may occur. The harm which is lesser should get priority over the harm which is greater.

To investigate both the principle of *wa^cd* and *wa^cdan* based on the above-mentioned maxim, table 3 below will examine the bilateral binding nature in *wa^cd* and *wa^cdan* in terms of *maslahah* and *mafsadah*:

Table 3: *Wa^cd* and *wa^cdan* in term of *maslahah* and *mafsadah*.

	<i>Maslahah</i>	<i>Mafsadah</i>
<i>Wa^cd</i>	<ul style="list-style-type: none"> - Preservation of wealth - Bank will never default in order to protect its reputation - The issue of <i>riba al-nasi’ah</i> can be eliminated 	<ul style="list-style-type: none"> - Open exposure - Fails to protect the right of customers since <i>wa^cd</i> only bind the promisor which is usually a customer. So, there is element of injustice to the parties involved - Does not give a perfect hedge
<i>Wa^cdan</i>	<ul style="list-style-type: none"> - Preservation of wealth - Both parties (bank and customers) is binding upon the promise <ul style="list-style-type: none"> - Give equal protection - -give justice to both parties - The issue of <i>riba al-nasi’ah</i> is eliminated since <i>wa^cdan</i> is not equivalent to contract 	<ul style="list-style-type: none"> - To some scholars, the binding nature on both parties may be equivalent to contract.

Table 3 shows that the even though the usage of *wa^cd* gives some *maslahah*, but the *mafsadah* is greater than *maslahah*. As compared to *wa^cdan*, the *mafsadah* in *wa^cdan* is lesser. Therefore, based on the principle of choosing the lesser harm, it can be concluded that the usage of *wa^cdan* is better than *wa^cd*.

Table 4: Below summarizes the illustration of table 3.

Aspect of <i>maslahah</i>	<i>Wa^cd</i>	<i>Wa^cdan</i>
1. Flexible	√	√
2. Need to be binding in order to ensure the stability of transaction	√	√
3. Preservation of wealth	√	√
4. Can be adopted in hedging products	√	√
5. Simple and straightforward	√	√
6. Least cost is needed	√	√
7. Does not require complicated transaction	√	√
8. Can avoid <i>riba</i>	√	√
9. Able to protect both parties	X	√
10. Equitable	X	√
11. Upholding justice	X	√
12. Perfect hedging	X	√

The table portrays that the harm consequences of *wa^cd* are much more greater than its benefits. *Wa^cdan*, therefore is a good alternative in structuring Islamic FX forward since the *maslahah* is greater than *mafsadah*. Even though *wa^cd* has many benefits such as simple, straightforward, flexible and able to preserve wealth, but the *mafsadah* in *wa^cd* is greater as compared to the *mafsadah* in *wa^cdan*. In this case, the usage of *wa^cdan* is better than *wa^cd* in terms of ability to protect both parties, equitable, upholding justice and providing a perfect hedge. As one observer stated "it is a requirement that buyers and sellers take protective measures against actual and potential harm (*darar*). *Wa^cdan* enable people to ensure that all products offered in Islamic hedging will bring satisfaction to all parties and then achieving a betterment for the whole community. Thus, *wa^cdan* has a great potential in developing Islamic hedging product and then achieving *maqasid al-shari'ah*.

The usage of *wa^cdan* is also consistent with the objective of Islamic finance which aims at contributing to the fulfilment of the socioeconomic objectives and the creation of a just society (Asyraf Wajdi & Bouheraou 2011). The usage of *wa^cdan* in Islamic hedging also has been proved that it can provide a perfect hedge and achieve justice, then all risks can be handled in ways favourable to build a just society. This is consistent with Islamic finance system that is a holistic system which aims at contributing to the fulfilment of the socioeconomic objectives and the creation of a just society (Asyraf Wajdi & Bouheraou 2011). Thus, Islamic FX forward is permissible if the transaction is done for genuine hedging purposes and have to be supported by appropriate documents to avoid speculation.

Since the principle of *wa^cdan* is dissimilar to a contract, therefore there is opportunity to develop a more innovative and sophisticated Islamic hedging products based on *wa^cdan*. Islamic hedging mechanism must be developed, so that risk can be mitigated effectively and at the same time preserving *maqasid al-shari'ah*. It shows that Islamic hedging solutions are integral part of the management tools required by all parties involved, including the Islamic financial industry.

Conclusion:

Since the protection of wealth is one of the higher objective of *shariah*, it may be argued that failure to protect one's property in the face of risk and bankruptcy is tantamount to neglect of duty which is undesirable from the viewpoint of Islam. Thus, Islamic hedging mechanism is vital in order to attain one of the *maqasid al-shari'ah*, which is preservation of wealth. FX forward, which is the common tools of hedging does not comply with *shariah* due to *riba al-nasiah* element. Hence, *wa^cd* is adopted in this transaction in order to eliminate the element of *riba*, so that the currency exchange does not violate *bai' al-sarf* rules.

It cannot be denied that the principle of *wa^cdan* in Islamic FX forward is flexible, simple to execute and does not require complicated transaction. However, under *wa^cd* structure, only one party promises to buy or sell as the case may be wherein he is bound by that promise. The other party is not bound by that promise however have to proceed with the promise undertaken by the promisor. Hence *wa^cd* fails to protect the right of customers if the bank does not want to honour the promise.

As an alternative to the application of *wa^cd* in FX forward transaction, this paper explores the viability of *wa^cdan* in the light of *maqasid al-shari'ah*. This paper proved that *wa^cdan* or two separate unilateral promises is distinguishable from contract, thus the views of saying that *wa^cdan* is equivalent to contract should be rejected. The application of *wa^cdan* will not raise issues of *riba al-nasiah* similar to the conventional use of forward currency contracts as it is not a contract. Then, a comparison was also made between *wa^cd* and *wa^cdan* and this paper found that the application of *wa^cdan* really achieve *maqasid al-shari'ah* better than the single use of *wa^cd* in terms of its ability to protect both parties, equitable, upholding justice and perfect hedging. Meaning that, Islamic FX forward using *wa^cdan* provides a better solution to customers who are looking for *shariah* compliant

hedging solutions which are prudent and equitable. The achievement of equality and justice in the transaction will lead to the stability of economy as well as the attainment of *maqasid al-shari'ah*.

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