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Shariah and Maqasid Analysis of Financial Derivatives and the Attempts to Islamize Them

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Abstract: There have been increasing attempts recently to Islamize some financial derivatives. These attempts were initially meant to provide solutions to certain problems like the need to buy a currency or some commodity at a predetermined price on a future date for hedging purposes, but they later developed to include using the same strategies for speculation purposes. The later development involves serious effects on economics, for speculations have been proved to be a major reason behind the occurrence of financial crisis. The paper analyzes the Shariah reasons for the prohibition of derivatives in general, and it shows in the course of the analysis the Shariah objectives relating to the particular Fiqh rules of derivatives. This is in order to help outline the Islamization standards of such instruments, if possible at all, which include the acceptability of the instrument used as well as its purpose and effect. Having outlined the standards, the paper seeks to apply them to the recent attempts of derivatives Islamization to determine their validity.

Keywords: Financial derivatives, Maqasid al-Shariah, Islamic finance, Islamic financial market, Islamization of financial products.

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1. Introduction

Financial derivatives are among the outcomes of financial engineering - the process of creating and inventing financial instruments and developing the existing ones. They are called financial derivatives because their value is derived from something else, i.e. they do not possess market value intrinsically, but depend on something that does. They may be considered as obligations initiated by the contracting parties on things that have market value, such as commodities, and then traded like real commodities. For example, the owner of a certain commodity may sell the right to buy this commodity from him for a specific price and delivery date; he commits to sell the commodity to whoever holds this right in accordance with the set price and delivery date. Hence, this buying right is a financial derivate resulting from the commitment [to buy or sell] a certain commodity, which is then traded in the market. To treat the above critical Shariah issue, the paper firstly adopts an inductive approach to examine all relevant Shariah issues, and then it shifts to the analytical methodology to achieve the research goals of weighing the financial derivatives from Shariah perspectives and the attempts to Islamize them.

2. Why the need for financial derivatives?

From the description above, it becomes obvious that financial derivatives may serve two needs: Firstly, they can be used to hedge against price change in the future. The buyer

who buys the right to buy the commodity at a future date for a fixed price protects himself from the risk of its price rising in the future. Secondly, they are instruments that can be used to speculate on prices with the aim of profit making. When used for speculation, the aim of the one who buys the right to purchase a certain commodity at specific price is not to actually buy the commodity in the future but to make a quick gain. Whenever the commodity price rises, he or she can sell that right for a higher price or wait until the sale execution date and claim the price difference from the original seller.

Today financial derivatives are very popular, with their market value at multiple times the value of the actual commodities that they represents (Hammad, 2001). They were originally designed for hedging purposes, but were later developed and used for speculation and trading. Nowadays financial derivatives are mostly used in financial markets for price speculation and not for hedging. According to a study published by the Office of the Comptroller of the Currency (OCC) in the United States, the percentage of trade in derivatives that actually ends in delivery of the commodities stands only at is 2.7% of their overall trade. In other words, only 2.7% of the total derivatives transactions is actually used for hedging, while the remaining 97.3% of derivative operations is used for price speculation (Sawilem, 2021).

3. Types of financial contracts

3.1 Forward contracts

In a forward contract parties agree to sell an asset at a specific price and delivery date. For example, a trader agrees with another to sell him 10 tons of wheat to be delivered on 1 June for a price of 50,000 dirhams that should be paid on delivery. Considering this contract as a derivative contract is untrue unless the obligation on behalf of the buyer or seller is sold in the contract. A financial derivate occurs when the seller's or the buyer's commitment is sold to the other contracting party or to a third party. These contracts do not occur in organized markets, which is what distinguishes them from future contracts.

3.2 Future contracts

Future contracts (or simply 'futures') are forward contracts that are conducted in organized markets - the financial markets. They are standardized contracts in the sense that they are subject to the rules of the organized market. This market is the guarantor of their implementation, and it solves the problem of finding contracting parties for a deferred sale of the desired commodity. In addition, it is the market, not the contracting parties, that normally sets the price of the commodities (Kunhibave, 2010).

In the markets of future contracts, the clearinghouses play the role of monitoring the price of the assets sold in the future contracts after the buyer and seller pay a specific margin. If the market price falls or rises, the clearinghouse requests the contracting party harmed by this movement to raise his margin to suit this movement. This is because these contracts have been developed basically for the aim of price speculation. The intention of the contracting parties in most cases is to speculate on the market prices, and not hedging. Hence, these contracts do not conclude with actual implementation of sale, delivery of goods and payment of the price, but by paying the price differences when the contract period ends. The loser pays to the winner the difference through the clearinghouses from the accumulated margin.

3.2.1 The difference between forward and future contracts

Although both are deferred sale contracts, futures and forwards remain distinguished from each other as follows:

The purpose of the forward contracts is usually hedging against price changes, so both contracting parties look forward to concluding the sale with actual delivery of the underlying asset, while the primary aim of the contracting parties in futures is price speculation and not the actual delivery of the underlying commodities.

The contracting parties set the conditions and obligations of the forward contract. Whereas future contracts are standardized contracts where the market sets the rules.

Forward contracts are usually effected on commodities. As for futures, they are on all the items that the organized markets have to offer, including commodities, shares, bonds, financial indicators and interest rates.

Futures contracts involve payment of some margin by the contracting parties under the supervision of the clearinghouse, which is not the case with forwards.

Settlement of the contract is concluded in forward contracts at the agreed delivery time of the contract. In contrast, futures contracts can be settled at any time before the specified date of the contract, in accordance with rules of the organizing market (Kamali, 2007).

3.3. Options

Options mostly relate to futures contracts, and they grant the holder of the option the right to pull out of the commitment to buy or sell a commodity at a specific price. In exchange for this option, he or she pays a price to the option seller. It is also possible in options, and this is most common, that they are initiated independently of any previous contractual obligations, so that they themselves include agreement on possible future sale contracts. In general, an option can be defined as: "a contractual agreement where the seller (the issuer of the option) grants the buyer (optionee) the right to sell to him or buy from him an asset at a predetermined price on a specified future date or at any time during the period ending on that date" (Hammad, 2001).

3.3.1 Types of Options

The most dominant options are:

Call Option

A privilege that gives the holder the right to buy a commodity or a financial instrument at a set price (the strike price) for a set term (the expiration date) in return for a set price (the premium) paid by the purchaser of that right to the seller (the writer). That is, the buyer of this right can choose between buying the commodity or the financial instrument at the agreed price and not buying it, within a specified period, which is usually three months (Hull, 2019).

From the above, it can be inferred that the buyer of the call option expects a rise in the market price of the commodity during the option period. He buys this option to either hedge against a possible raise in price of the commodity he wishes to acquire or for gaining through price speculation, as shall be discussed shortly. On the other hand, the seller of the option expects the price to remain stable during that period; not a fall or else he would sell his goods now, and not a rise or else he would not have given this option, so he earns from the price of the option that he sold.

Put Option

The put option is the opposite of the call option. It gives the holder the right to sell a specific commodity for a set price during a set period, in return for a known sum that he pays to the other party.

Therefore, the one who buys this option among commodities owners is a one who fears a price fall in the future during the period of the option. On the other hand, the one who sells this option expects that the prices will not change during the option period, since he would not consent to sell that option if he expected a fall in the price, while he knows that the buyer of the option would sell the commodity to someone else if the price raises (Hull, 2019).

Similar to call option, the buyer of a put option is motivated either by hedging against a price fluctuation of the commodities that he wishes to buy, or motivated by price speculation.

Naked Option

The seller of a 'naked' option does not own the commodity that he, for example, sells the right to buy to others. This option is termed so because it is unconnected (naked) to

any asset that the seller owns. The aim of the seller of this option is speculation on the price of the underlying commodity as he owns no commodity to hedge against a fall in its price (Hull, 2019).

3.4 Swaps

A swap is an agreement between two parties to swap payment obligations, cash flows or returns of assets or financial instruments for a fixed period. It may include swapping a variable return for a fixed return, or swapping a return on one currency for a return on another, or swapping a variable return for a variable return, such as equity swaps.

To clarify, someone who receives a variable return from investment assets, such as shares, or a variable interest rate from a debt certificate can swap it for a fixed return, such as rent from a property, for a set time, such as a year. Hence, each receives the other's return for that period. One may also have a return in a certain currency, such as in euros, and fears a fall in the value of the euro at a certain time so he prefers to receive dollars instead. Hence, he makes an agreement through an agent with someone that has the opposite intentions/expectations. They swap their returns in the two currencies [currency swap]. A commodity swap occurs for example when the price of a million barrels of oil is swapped over a specific period of time for a fixed specified amount. The seller of oil has guaranteed a fixed return for his oil, but have lost in return the chance to achieve higher profits if the price of oil rises (Hull, 2019).

These examples refer to using swaps with the aim of hedging, although in reality they are mostly used with the aim of price speculation, whereby the transaction concludes by settlement between the winner and the loser.

4. The Fiqh issues related to financial derivatives

From the aforementioned description of financial derivatives, we can determine the main jurisprudential issues as follows:

Deferring the both counter-values of a sale contract

Future sale of currencies and financial instruments.

Sale of al-khiyār (option), then trading it with others.

Deferring the sale of cash with an unknown counter-value.

Speculating on prices in the markets.

4.1 Issue One: Deferring both counter values in sale contract

Deferring counter-values in a sale is known as impermissible in the Shariah, and the prohibition relates to two reasons: gharar (uncertainty) due to the possibility of failure to deliver the deferred values in the future; and riba, if there is an increment in the counter-value being deferred. This is because, in principle, deferral may be in one or both of the counter values. If the deferral is in one value, then the matter relates to gharar, and it also relates to riba if the counter-values are of the same genus while the postponed value is higher than the spot value. To elaborate, the deferred value could be either the commodity, sold for an immediate cash payment - which is the case of salam; or it could be the price while the commodity is delivered spot. Both cases involve gharar given the possibility of failure to deliver the deferred value on the agreed time. Nevertheless, Shariah has tolerated the uncertainty associated with such a sale in view of it being a general need. Salam facilitates production and benefits both contracting parties. Deferred payment sale meets a general need as well, as many people cannot afford to buy on cash basis.

On the other hand, deferring both counter value involves double-sided unnecessary gharar, and there is no general need that would justify or tolerate it. It has been reported that "The Prophet, peace be upon him, prohibited selling al-kāli' bi al-kāli' (deferred for deferred)". Despite the questionable authenticity of this hadīth, Fiqh schools unanimously rule deferral of both counter values as invalid.

In fact, the wisdom behind the prohibition of deferring both counter-values also relates to blocking the door on speculators and gamblers, whose practices lead to destabilizing and the economy and the prices of commodities. This is evidenced by the fact that the Shariah provisions relating to deferral of the sale values gets stricter whenever the underlying assets are important. For example, the sale of currencies and the ribawi commodities is subject to strict Shariah rules in view of their significance and importance. (Abozaid, 2021)

Undoubtedly, this wisdom nowadays is more evident today than ever before, and perhaps it is clearer than the wisdom associated with interpreting the prohibition by the uncertainty (gharar) resulting from the possibility of the contracting parties' inability to implement the deferred contract. The regularity of the markets today, the abundance of goods, and the market guarantees of contracts implementation almost eliminate such uncertainty (gharar). From this particular regard, gharar could be tolerated nowadays, but what remains unresolved is the more serious application of gharar, which is gambling through price speculation with all of its negative economic effects.

In conclusion, it can be said that, in principle, it is not permissible to enter into a sale where both counter values are deferred. This eliminates the legitimacy of forward sales contracts (Forwards) and future contracts (Futures), especially since futures contracts, similar to options, have been designed to facilitate speculation.

4.2 Issue Two: Future sale of currencies and financial instruments

Commodities are not the only items that are purchased and sold in forward and futures contracts. Currencies and financial instruments such as shares and anything that has a volatile value or a volatile financial reference such as the interest rate, financial indices and cryptocurrencies could also be included.

The previous discussion on deferring both counter values in a sale contract implied the prohibition of future sale of currencies due to the gharar (uncertainty) involved in the contract, but more importantly due to the possible speculation (gambling) on the currency values. Such speculation impairs the known economics functions of currencies being a means of exchange, a unit of account and a value-store unit. Obviously, in order for currencies to efficiently play their perceived economic roles, they have to maintain a relatively stable value, while excessive speculation would necessarily cause high volatility in their values. It is for this reason, among others, that Shariah prohibited future sale of currencies and deemed it a kind of Riba (Abozaid, 2021).

As for financial instruments, such are shares, there is no reason to condone their future sales since their future sales is perceived to be for speculation only. Rather, the sale of shares in general must be subject to certain restrictions to remove the speculative nature that affects their market price as a result of several practices, such as short selling and margin trading, especially in the absence of adequate control and oversight by the market supervisory authorities.

With regard to financial indices and interest rates, irrespective of their underlying impermissible transactions, they are simply numbers, and do not have an intrinsic value, such that they can be bought and sold. Of the essential conditions of every sale item according to Shariah is that it should constitute wealth (māl), that has a value, and that it should be mutaqawwam, i.e. it has a value that is recognized by the Shariah. This is because there are things that people may regard as valuable but are not valuable according to the Shariah, such as alcohol and pork. In addition to financial indices and interest rates not achieving the characteristic of mal (wealth/value), buying and selling them through derivatives trade makes the operation akin to gambling. Both the seller and the buyer gamble on the movement of the number (the index/interest rate) in a certain direction, up or down. The one whose expectations prove right earns a certain amount payable by the counter losing party, just like betting on the result of a football match or a horse race.

In this context, it is worth noting that OIC Fiqh Academy passed a resolution on the impermissibility of buying and selling financial indices, stating: "The index is an account number calculated in a special statistical way intended to know the extent of change in a particular market, and it is sold in some international markets. It is not permissible to buy and sell the index for it involves pure gambling as well as the sale of something fictitious and does not exist".

4.3 Issue Three: Sale and trading of Option

In Islamic financial law there is the so called "option of stipulation" (khiyār al-shart), which is: a right that the seller or buyer conditions during the transaction allowing him to reverse the transaction within a specific time. Some jurists have restricted it to three days, others to one month, while others considered it a matter left up to the contracting parties to agree on. The basis of this option is the Hadīth narrated by Hibban bin Munqith, who complained to the Prophet, peace be upon Him, that people used to take advantage of his limited market skills. The Prophet responded: "when you conclude a sale you may say that there must be no fraud, and that you reserve for yourself an option lasting three days".

While this option is free of charge and it cannot be compensated for and hence, it cannot be used as a basis for the conventional option, 'urbūn n the other hand seems usable. Some jurists allowed (what is known in fiqh as) bay' al-'urbūn, which is a sale including a right given to the buyer to nullify the sale during a specific time in exchange of an amount paid to the seller. If the buyer goes ahead with the purchase, what he paid shall be considered a portion of the sale price; but if he does not, it is forfeited and it goes to the seller.

However, even if we accept the position permitting 'urbūn sale, the differences between it and the conventional options remain large, which prevents justifying conventional options on the basis of 'urbūn, as shall be discussed soon. Besides, this option ('urbūn) is simply a right relating to the sale or purchase, and not something that can be traded independently.

In this context, it is worth noting that OIC Fiqh Academy ruled that the issuance and circulation of financial Options is prohibited: "Contracts for options - as currently applied in the global financial markets - are new contracts that do not fall under any of the known Shariah contracts. Since the subject of the contract is neither a sum of money not a utility or a financial right that is permissible to be exchanged, then it is not a permissible contract from a Shariah perspective. As these contracts are primarily prohibited, their handling is also prohibited".

4.4 Issue Four: sale of deferred cash with an unknown counter-value

It is obvious that swapping returns involves sale of money for money. If of different currencies, the transaction involves riba al-nasī'a only, while if the two counter values are of the same currency, then Riba al-fadl also materializes due to the inequality in the sums of the two values. Hence, riba of sale (riba al-buyū'), which includes riba al-fadl and riba al-nasī'a, invalidates the swap of returns. However, in addition to the occurrence of riba of sale, gharar (uncertainty) befalls the unknown value in swap of return. Hence, swapping a fixed for a variable return encompasses the two evils of both riba and gharar, rendering swaps worse in terms of invalidity than the other derivate contracts.

4.5 Issue Five: speculating on prices through derivatives

Current market conditions show that the main aim of dealing in financial derivatives is not hedging, but rather speculation on their prices through the circulation/trade of these derivatives. The original sale contract is not intended in trading derivatives as the matter concludes with settlement and payment of the difference in prices to the winner in this trade, without a real exchange of the underlying assets.

Thus, irrespective of the specific Shariah rulings pertaining to these derivatives, the intention of the contracting parties must be considered when passing judgement on these transactions. Derivatives when intended for speculation involves zero-sum game; what

one wins is the amount that the other loses. This amounts to gambling, as it involves two parties making an agreement to pay only the party whose expectations about the market performance turn to be correct, which is the very essence of gambling.

By considering the effects of dealing in derivatives on the economy and the society, their potentially catastrophic effects outweigh any benefit that may be derived from them. Ownership of the underlying asset is not even a condition in trading derivatives, making derivative trading an easy field that can be accessed simply by paying the market entrance fee or the price of the derivative that is bought to be speculated upon, even if the price of the underlying asset is in millions. This has caused the size of derivatives trade to reach astronomical figures, which exceeds real trade in the world by multiple times. This huge amount of speculation on prices of commodities and currencies leads to high level of price volatility (Obaidulllah, 2012).

In fact, using derivatives for speculation stands contrary to the original idea behind the very invention of derivatives, i.e. hedging. This is because derivatives have led to an increase in risk and price fluctuation of commodities in the market. Paradoxically, as derivatives increase in volume, the risks (volatility) increases, which in turn intensifies the need for hedging!

In summary, dealing in financial derivatives incurs in their totality some of the greatest Shariah violations pertaining to financial transactions, including riba of sale, riba of debt, selling what is not owned or possessed by the seller, selling things of no value on their own, gharar and gambling. Thus, derivatives transactions include most of the prohibitions that may befall a sale contract.

5. The attempts to Islamize financial derivatives

The paper has so far discussed the various types of financial derivatives and the Shariah rulings related to them. Now it turns to discuss the attempts to Islamize financial derivatives from a fiqh and maqāsid perspective.

In recent times, various actors have embraced and competed in developing financial derivatives after the latter have grown in importance and in number exponentially.

The first attempt to Islamize derivatives was when Islamic financial institutions attempted to find a way to fix the price of currencies needed at a future date to hedge against unfavorable changes in the exchange rate. The conventional way of doing so is through forwards or futures in currencies, which are prohibited contracts, as discussed. This necessitated finding a Shariah-compliant alternative for buying currencies in future and fixing the exchange rate.

Al a latter state, attempts were even made to Islamize swaps, i.e. swapping obligations of variable for fixed payments/returns. As pricing in long-term financing by Islamic financial institutions is linked to the variable interest rate, such as in ijarah ending-in-ownership, there was a need, especially for clients, to change the obligation of a variable instalment payment to a fixed instalment payment.

Further attempts were later made to swap returns and cash flows in order to attract more investors by giving them guaranteed and more stable returns.

These are the most notable derivatives attempted for Islamization so far, but Islamic financial institutions, as well as Shariah advisory firms, are competing to expand the scope of Islamization in field of derivatives, in order to attract more customers and achieve higher profits.

However, it can be argued that these attempts to Islamize derivatives have not followed the necessary methodology required to Islamize a financial product. This methodology relates to ensuring the Shariah soundness of the instrument/contract used for Islamization, as well as the soundness of the essence, effects and results. Discussion of this matter is in the following.

The deficiency in Islamization of derivatives in terms of the instruments used

Some of the tools and instruments used in Islamizing derivatives are invalid in essence, while others are valid in essence but they have been twisted or misused, as follows:

5.1 Use of Tawarruq or 'īna

'īna refers to a process that involves a collusion between two contracting parties for one to sell the other a commodity on a differed payment basis – say 60 - then to buy it back from him immediately for a lower spot amount – say 50. Hence, the one who bought first on credit then sold on cash receives cash and becomes indebted to the other by the higher amount deferred. It is equivalent to lending 50 for 60, whereby the technicality of the sale contract is nothing but a subterfuge. In tawarruq this process occurs with a third party. Hence, the buyer for 60 deferred sells to a third party for 50 spot, and not to the first seller, but again with collusion between the parties involved.

All jurists, including the Shafi'īs, are in agreement that 'īna, as described above, is an impermissible sale, but they differ over its validity as a sale contract. While Shafi'īs and Hanafīs base the contract validity on its structure regardless of any other consideration, Malikīs and Hanablīs base the contract validity on its structure as well as essence, purpose and implication. Consequently, 'īna would be ruled as valid by the first group of jurists in view of its valid structure being a sale contract, while it would be ruled as invalid by the second group in view of its essence being a subterfuge to rib. As for tawarruq, some of its formulations were deemed permissible in the Fiqh literature ; however, the forms applied by Islamic financial institutions nowadays are different and cannot be condoned on Shariah basis, because they are no different from 'īna in effect. Both'īna and tawarruq yield exactly the same end result, and this is the very reason why OIC Fiqh Academy has issued a resolution prohibiting all form of the tawarruq used by Islamic banks.

Both sales, 'īna and tawarruq, have been used to Islamize derivatives such as swapping variable financial obligations for fixed ones. For example, if a client is obliged to pay variable instalments, such as rentals in ijārah ending-in-ownership to the financing bank, and he would like to swap it with fixed instalments, fearing an unexpected increase in the underlying variable of the rentals, which is effectively the interest rate, then the following formula is presented. Before the payment period for the variable instalment is due, the client signs a tawarruq contract with the bank. The client sells the tawarruq commodity (that the bank buys for him on an agency basis) for a price equal to the instalment that needs to be paid, and which was unknown (variable) but it is known now. The bank then sells the tawarruq commodity for a spot price in the market, and instead of forwarding the price to the client the bank sets it off against the 'variable' ijārah instalment that is due to be paid to the bank. In this way, the client's problem of paying a variable instalment is solved. However, to arrange payment of fixed instalments to the bank, the client executes another tawarruq/'īna contract with the bank whereby the bank sells a commodity to the client with known fixed instalments, such that each instalment equals the fixed amount that the client wishes to pay instead of the variable installment.

However, both contracts, 'īna and tawarruq, are impermissible as highlighted earlier and as such, all transactions involving them become unlawful.

5.2 Use of Promise

A promise to sell was used as an alternative to a sale contract in financial derivatives, because a promise is not considered a contract in the Islamic Shariah due to it not being binding. Therefore, the parties promising to sell or exchange currencies should not contravene the Shariah if they promise to sell a commodity for a certain price on a certain date, or promise on a currency exchange on a certain date.

Investigation of the Fiqh literature on the matter of mutual promises on the exchange of currency shows that while Mālikis prohibit it due to its resemblance with a contract, Imam Al-Shafi'ī and Ibn Hazam permit it whether the price of the currency is determined in the currency or not. The reasoning they give is that a mutual [non-binding] promise on

the exchange of currency does not amount to a currency exchange contract such that it may be prohibited for lack of spot payment.

Nevertheless, OIC Fiqh Academy passed a resolution prohibiting deferred currency sale and prohibiting mutual promises on a currency without distinguishing between binding and non-binding mutual promises.

Some contemporary fatwas, however, permits the two contracting parties to give mutual promises that binds one party only. This is based on the reasoning that since the agreement binds one party only, it is not a contract as a contract typically binds both parties.

This reasoning is, however, questionable as it opens the door for justifying the use of derivative contracts for various aims, including speculation . Besides, the application of this mutual promise for hedging is an impractical solution, and does not achieve its intended aim since it binds only one party, giving thus the option for the other contracting party to back from the agreement.

5.3 Use of 'Urbūn sale

Among the instruments used to Islamize financial derivatives is the 'urbūn sale, and as mentioned earlier, some jurists permit it. It is a sale that guarantees the right of the buyer to nullify the sale during a specific time, but the buyer must pay a certain amount to the seller; if the buyer goes through with the sale, the amount that he paid is included in the price of the sale item, but if not, it goes to the seller.

As 'urbūn consists of [selling] an option to buy for money, it has been considered a sound basis for justifying the Islamization of conventional financial options. If it is permissible in the Shariah to get an option in return for money at the start, why would it not be permissible to sell this option to someone else, and for it to circulate in the same way that occurs in options in financial derivatives!

However, even if we hypothetically accept 'urbūn, following the Hanbali school of thought, the differences between the 'urbūn sale and conventional options remain significant, which cuts the relationship between one and the other.

The differences are the following:

What is paid in 'urbūn is not the price of an option. If it were a price, the seller would deserve it whether the buyer goes ahead with the sale or not. Rather, it is compensation for the seller if the buyer chooses not to conclude the purchase, while if the buyer chooses to go ahead with the contract, the 'urbun is part of the sale price. As for a conventional option, the amount that the buyer pays for the option is not a portion of the sale item but is an independent price for it. Hence, 'urbūn does not involve buying an option for money.

The option in 'urbūn sale is restricted to the buyer since he is the one who effected the sale agreement with the seller; the buyer cannot substitute another buyer in his place through the 'urbūn, whether through sale or gift. In other words, the option included in the 'urbun is an effect of the contract that has been signed between two specific contracting parties as a result of their contract. Selling or bestowing this implicit option amounts to changing one contracting party for another, which is not allowed, because changing the contracting party is equivalent to changing the very contract. In order to replace a contracting party, the first contract would have to be nullified and a new contract would have to be initiated with the new contracting party if the other party agrees. If the contract becomes invalid (fāsid) due to changing the contracting party in the same contract, so do become its legal consequences and effects - including this right, i.e. the right of option in 'urbun.

Hence, the 'urbūn is not a right that can be bought in exchange for money or traded. As such, it does not resemble conventional options such that they can be justified on its basis.

The above differences relate to the essence and concept of 'urbūn in contrast with the financial options. As for their practical application, various differences make clear the differences between the two.

They are the following:

'Urbūn occurs in a sale without deferral of counter-values, while conventional options are in deferred sale, which is prohibited in the Shariah, as previously discussed.

Passing the time of the option in 'urbūn, like in khiyār al-shart, without exercising the implicit option makes the contract binding, since a sale contract is originally binding. As for conventional options, if they expire, no sale contract takes place.

Hence, 'urbūn is not a sound instrument for the Islamization of derivatives due to the large and significant differences between the two. In addition, an option is not something that can be sold in the Islamic Shariah, because it is a mere right related to buying and selling, and not a wealth (mal) that can be exchanged.

6. Lack of conformity of the Islamized derivatives with Shariah in terms of their objectives, aims and results

As highlighted earlier, the first attempts to Islamize some financial derivatives were for the objective of finding legal exits (makhraj) for real problems, such as the problem of needing to buy a currency or necessary raw materials at a certain future date. At a later stage, the attempts geared towards not addressing a real need, but giving legitimacy to some market operations designed for speculation (gambling). What is unfortunate in this regard is to acknowledge the harms of conventional financial derivatives and the wisdoms for which our Shariah has prohibited them, as indicated earlier, and yet attempt to Islamize them! These attempts strip Shariah rules of their wisdom and render them meaningless. In fact, the recent global economic crises have provided us with practical evidences to the dangerous and destructive role of these derivatives (Birch, 2009), which confirms the wisdom of our Shariah rules. It is also unacceptable to promote Islamization of derivatives on the assumption that they are used for hedging purposes, and then to turn a blind eye to the reality of their practical usage, which is mostly for speculation purposes - counter to what their engineers claim.

Furthermore, hedging itself does not justify overriding Shariah rulings using controversial instruments such as 'īna and tawarruq. The Shariah has defined specific instruments to hedge in sale contracts, such as option of stipulation (khiyār al-shart), option of non-payment (khiyār al-naqd) , option of determination (khiyār al-ta'yīn) , non-binding promises from any of the two parties as well as 'urbūn, which is valid according to some jurists. Thus, while people have the right to engineer new hedging instruments that suit the contemporary financial needs, they must do so without violation of Shariah rules by using inappropriate instruments.

In addition to the soundness of the instruments used in hedging, the effects of hedging operations must be carefully examined and assessed as well. There could be no general economic benefit in the widespread fixation of commodities future prices, but rather subtle economic harms. It is not unreasonable to assume that excessive hedging could affect market competition and lead to price inflation. The Prophet, peace be upon him, refrained from fixing the prices of the commodities when he was asked to do so , and fixing prices is a strong form of hedging.

It is also important not to forget that certain market risks that require hedging have arisen due to conventional practices that are not Islamic but have been practiced in Islamic finance. Islamic financial institutions price their long-term financings usually in reference to the interest rate, which may vary sharply, such as in ijārah ending in ownership, where each installment payable by the financee (lessee) comprises a fixed rent representing the proportionate amount of financing, and a variable rent representing the bank's profit, which is related to the interest rate. This practice creates real risk for the client, as the interest rate could increase unexpectedly, which places him in financial difficulties that need to be hedged against. It also creates a problem for the financier if the interest rate

falls unexpectedly, leading it to hedge against these risks. This questionnable practice has created an unnecessary risk to hedge against through swaps that use ʻīna or tawarruq, as already explained. Actually, the invalidity of the said practice stems from the excessive gharar; the lessee is unaware of how much rent he will have to pay, and could end up paying more than he or she expected, due to an increase in the interest rate. Similarly, the lessor does not know how much he will receive, since the interest rate may fall below his expectations. Such excessive gharar could be simply avoided by sitting a minimum and maximum limit for this rate. By doing so, the excessive gharar that invalidates the contract is overcome, and there would be no excessive risk for parties in this transaction to hedge against.

In summary, it is necessary for the aim or use of the derivative subject for Islamization to be permissible, such that it is not meant to justify a prohibited practice like price speculation or swapping returns or payment obligations. Obviously, price speculation through derivatives involves gambling and return swaps involves unlawful sale of money for money, as discussed earlier.

7. Conclusions

In final analysis, the gharar problem with a future sale does not lie in the possibility that such a sale may not be eventually concluded due to the failure of the contracting parties to do so. If this were the reason, then it would be valid to say that this problem no longer occurs in contemporary organized financial markets nowadays, were everything is well regulated to the extent that would eliminate the possibility of failure to conclude a contract. Rather, the big problem is in the essence of these transactions that may not differ from betting and gambling, and in the negative economic consequences connected to them. The Shariah texts radiate in every age with new meanings that may not be known or understood except by the people of that age. This may be a reason why many of the texts have remained with their reasoning left unexplained. They come is an imperative or proscriptive form, requesting the followers of the Shariah to abide by them without clarifying the reasoning, because they open to new meanings that makes it unsuitable to extoll the reasoning behind them at their advent. The wisdom behind the prohibition of a sale of deferred counter-values, for example, was perceived as protection of the contract, since non-delivery of both counter values involves excessive and unjustified risk. When implementation of such contract became commonplace and guaranteed in the organized markets, another wisdom behind this prohibition emerged, which is using this contract to speculate in a way that produces even a greater a harm than that of a failure to deliver or pay the counter values. It is the harm of gambling, which befalls the gamblers as well as the society as a whole as it leads to artificial pricing of commodities.

The paper also records the following results:

- Failure to realize the wisdoms and objectives of certain Shariah rulings has led to failure to genuinely observe and implement those rules, which in turn caused a failure to restrain the evils the rules came to prevent.

- Attempts to Islamize derivatives have mostly relied on unacceptable tools and have yielded products that are in conflict with the objectives of their corresponding Shariah provisions.

- Conceptual differences between ʻurbun and the financial options deny the possibility of their justification on its basis.

- Swapping returns or financial payment obligations is not acceptable to Sharia, for they involve future sale of money for money, with one or the two counter value being unknown in amount.

- Some of the controversial practices of Islamic financial institutions have created novel risks, which prompted the needs to hedge against.

- In principle, hedging is permissible in Shariah, but it should be through use of legitimate means and tools, and it should not lead to any Shariah cautions or cause economic harms.

- Finally, the paper warns of the importance of conducting a Maqasidi study of all Islamic financial transactions, in order to highlight the purpose and objective of each ruling, because not doing so has led to misunderstanding many Sharia rulings, and the attempts to Islamize the unislamizable. This is especially feasible at our present time with the numerous lessons that can be learnt from the global market practices, which left nothing untested. Indeed, the market practices have provided us with extremely important tools to understand our financial jurisprudential heritage, thus helping us to realize the objectives and goals of these rulings.

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