

Islamic options (al-Khiyarat); Challenges and opportunities

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Abstract. In Islamic finance text, options are called by *al-khiyarat*. The different investigators presented various numerous of their cases, but we try to discuss whole types of them. We review the Islamic options. Furthermore, this study is presented in three parts, one of which provides a review of the Islamic rules related to *al-Khiyarat*. Next, discussion about challenges of *al-Khiyarat*, finally addresses the study on developments of options in Islamic finance.

Key words: Delivery, Islamic finance, Options, Trading

1. Introduction and outline

Islamic financial have developed in dimensions and value in the previous decades. Islamic financial institutions activate in excess of 60 countries, and they use around \$100 billion of assets. In the majority of them, they run along with traditional financial institutes, however there are some countries where only Islamic banks are permissible [1].

Qur'an and *sejarah* are main resources of *shariah* that is Islamic laws. It includes Muslim's activities in the entire of the lifetime, For instance, social, economic, and so on [2]. Islam is a comprehensive method of life and presents the main way to solving all the troubles of humankind, as well as the economic problems. It is related to the group or Muslims (in any case) to know the values, interpret acceptably and give useful solutions to the humanity [3].

Resource recruitment in all ways of the Shari'ah suggested potential should be extended to generate a relation between financial aggregates and real dynamic actions [4]. There are some factors that they have effect on the growing of Islamic finance, Such as the liberalization of capital movements, privatization, the global integration of monetary markets, and the presentation of innovative Islamic products [5].

One of the main instruments for financial derivatives is the option. It's giving the right to the buyer (or seller) to sell (or buy) with clear price at the predetermined time. Respectively, option used in Islamic finance at the same performance and different name (*al-Khiyar*).

The outline of this paper is as follows. We will study specific kind of options, which is often recalled to as an Islamic option ("*al-Khiyarat*"). Next we study on the challenges of Islamic option (*al-Khiyarat*). Finally, we investigate some factors for development of *al-khiyarat*. Section 6 concludes the paper.

2. Preliminaries and review of Islamic Options (*al-khiyarat*)

Option is one document that it gives right to the holder (not the obligation) to buy (or sell) at pre-determinate time and price. We called this price by the strike price [6]. The Quran is the main source of Islam, including the terminology of God as delivered to the prophet Mohammed (pbuh) while the Hadith

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consists of story minutes of the events and sayings of the prophet himself. Ijtihad is the third Shariah source that the origin and formulation of Shariah laws by practiced scholars [7].

An option is one of the main financial security that giving the right to buy or sell an asset, with predetermined time and price [8]. In this paper, we will be focus on shariah-compliant option, which is often called Islamic option (*al-Khiyar*).

Our approach In this paper is Islamic options that they compliance with Shariah. Islamic option encompasses some types of rights (not obligations) that have financial concepts, *al-khiyar* generally divided to some types that its can validate or cancel the contract base on Shariah.

In Islamic finance text, options are recalled by *al-khiyarat*. The different investigators presented various numerous of that, but we try to discuss whole types of Islamic options (*al-Khiarat*) under the traditional shariah laws (*fiqh*). They are *khiyar al-shart*(option as a condition), *khiyar al-ayb*(Option from Defect) , *Khiyar al-tayeen*(Option of Determination or choice), *khiyar al-ruyat*(Option of Inspection), *khiyar-al-majlis*(Option of Meeting/Acceptance) ,*Khiyar al- Ghabn*(Option of Deception), *Khiyar al-Taakhir*(Option of Delay), *Khiyar Kashf al-Hal* (Option of status), *Khiyar al-Naqd* (Option of payment), *Khiyar al-Qabul* (Option of Accept) and *Khiyar al-Taghrir* (Option of Fraud) [9] [10]. We show the Islamic options structures as the following (fig.1):

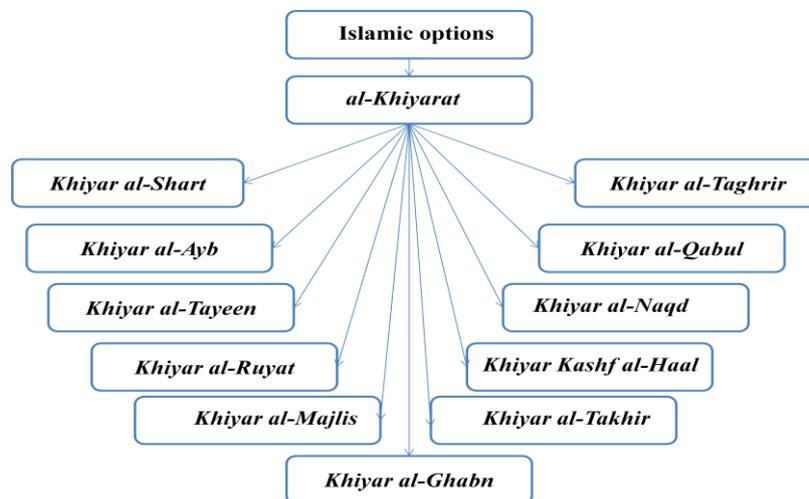


Fig.1: Structure of *al-Khiyarat*

3. Challenges of *al-Khiyarat*

There are numerous challenges that confront scholars who consider Shariah-compliant for options. We will attempt to present some of them in this part. One of the main challenges in *al-Khiyarat* is the time. It is included time of *aqd* (time of contract) and time of delivery. For instance, the trading could be canceled in the *khiyar al-shart* or *Khiyar al-Taakhir*. Another challenge for Islamic option is conditions of contract. In any ways, if whole conditions of the contract have not been satisfied, then the contract can be cancelled (*faskh*). Furthermore, cancellation could occur by parties of trading with the agreement to how exercise. As the following we study on some challenges with the applied approach.

In *Khiyar al-Tayeen*, the buyer face to the some options to choose, and he must apply the design making to get the optimal benefit.

There are a number of problems that require related to options to be permissible under the *Shariah*. Such as exclusion of gambling (*maysir*), redundant risk taking (*gharar*), and of transactions based on unawareness (*jahl*), trading in allowable (*halal*) goods only[11].

In Islam, *Maslahah* means all activity with the purpose of promoting the communal happiness. That bases of *Quran* and *Sunnah* of the holy Prophet Mohammad (pbuh) [9]. Some basic aims of *Maslahah* are fair buy (or sell), legal trade of assets any try to restrain the monopolistic tendency. The opposite of *Maslahah* is *mafsadah* (evil) [12].

Islamic option will forbid trades by *al-gharar*, that implies deceit or uncertainty in trading. One solution for the decrease the *gharar* in option is the *al-ikhtiyar* in trading, and its result is Islamically suitable restriction. One of the main benefits of Islamic option is reduced the opportunity of conflicts between the traders because with *al-ikhtiyar* their incorrect decisions are minimized [12].

The *Khiar al-Ayb* active only after found the imperfection in the case of trading. In addition, everything that caused reduced in the value and as a result in the market. This option is valid when the purchaser comes to recognize of some defect in the article of sale. Thus, he shall cancel the agreement or re-fund the price of trading [13], [14].

There are three main conditions to implement *khiyar al-ayb*. First, that defect occurs at contract time or before that. Second, this defect should due to decreases its price. Finally, the customer must be uninformed about that defect before the delivery of commodity [15]. If the seller show that defect of commodity before trading or lack any condition same this in his contract, the trading is correct (*Sahih*) [16].

There are some properties to exercise the *khiyar al-ayb*. The buyer knows the defect, before the trading the seller transfer the right of this option to other and the change by this price after clear the effect is very less [17].

4. Development of *al-Khiyarat*

Islamic finance is growing recently [2]. Numerous of markets, especially in Muslim countries tend to use the Islamic conditions in their trading. On the other hand, it seems that necessary to survey of factors that help to extend of *al-Khiyarat*. The future expansion of the Islamic options will depend on the creation of novelty in the financial instruments. Two main tools for that goal are financial and human resources [9].

Islamic trading had seen more in the Middle East, Arab countries and some Muslim countries in south Asia. For instance, in Malaysia, some Bank presents the special services for Muslim customers. Furthermore, Compared to traditional trading, the new Islamic trading are more flexible than classic trading.

Development of *Shariah*-compliant trading related to some factors such as dynamism of the *fiqh*, extend of Islamic financial techniques and concepts of laws. Some organization (for example, the Islamic Financial Services Board (IFSB) and other Islamic financial institutions) tries to clear this environment to traders by specification of standards criteria. They endeavor to the regularity of trading based on *Shariah*. For this case, lately some organization was set up to help the Islamic financial corporation's by specification of acceptable trading [11].

Despite that development, there are few numbers of countries where they have the complete structure according to *Shariah*-compliant. Before Islamic finance is derived by *fiqh*, and show clearly that income should not be granted for return [2].

There are two main factors for trend of Islamic countries to *shariah*-compliant trading. First, one is the growing of capital in development and industrial countries. Second one is the displeasure about that traditional system and tends to have the new opportunity with growing of floating liquidity [5].

The literature showed an Islamic option can be an essential for Islamic and non Islamic countries by *Shariah*-compliant trading that are kept out of loss of seller and buyer. That means will gain the pre-determine goals. 4 Performance assessments is a main requirement for growth of any cases [4].

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6. Conclusion

Islamic finance could be help for managing the trading. There are some challenges for trading under Islamic laws, but many Muslim countries tend to use this type of financial activities. To keep away from *Ribah* (interest in financial market), usually the Islamic Banks manage their resources by profit-sharing. Islamic finance could present suitable services if they are compliance with *Shariah* and policy. The growing of Islamic finance requires professional's persons who are now both of trading techniques and condition of *Shariah* [18].

There are two main results from this paper. First, decrease the *jahl* causes increasing the beneficial trading and efflorescence of Islamic markets. Second, despite it was seemed, the Islam due to limitation in financial activity, *al-Khiyarat* help to development of using the whole capital in the world and development of monetary instruments.

This will help the customers to create an opportunity for beneficial activity that it is *Shariah*-compliant. Although, there are some challenges for Islamic options, but development of Islamic options will be the key for growth of trading in Islamic financial market and becoming a good international power. We hope that this investigate will help the traders in Islamic finance by better understanding with a *figh* perspective.

7. References

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