IIFM GUIDANCE MEMORANDUM AND PRODUCT DESCRIPTION

مذكرة توجيهية إرشادية ووصف المنتج

for

Master Terms and Conditions
for an Islamic Foreign Exchange Forward (Wiqayah Min Taqallub As'aar Assarf) (IFX)

Two Unilateral and Independent Wa'ad based structure &

Single Binding Wa'ad based structure

للشروط والأحكام الرئيسة لاتفاقية الود بالصرف في المستقبل (وقاية من تقلب أسعار الصرف)
القائم على هيكل وعدين منفصلين مختلفين المورد من طرفين
و القائم على هيكل وعد ملزم من طرف واحد
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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

In the Name of Allah, the Most Gracious, the Most Merciful
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1. PURPOSE AND STRUCTURE OF THESE GUIDELINES (THE GUIDELINES)

The purpose of these Guidelines is to highlight the key operational aspects of proposed forms of agreements for standardised Islamic Foreign Exchange Forwards or Wiqayah Min Taqallub As'aar Assarf (“IFX”) which are Wa’ad - based and involving either a two Wa’ad structure or a single Wa’ad structure (the “IIFM IFX Agreement”) developed by IIFM and ISDA for use by Islamic financial services industry (IFSI) participants. These Guidelines are not intended to be exhaustive and are documented to provide clarification on key operational aspects. In many cases, the analysis will help to identify the key issues that may need further consideration by the counterparties to the contract.

The defined terms used and the references made in these Guidelines are to be read in conjunction with the definitions and the detailed clauses contained in the IIFM/ISDA IFX Agreement.

Further analysis and interpretation will be needed in order for an Islamic financial institution (“IFI”) to consider the potential impact of these Guidelines in light of each IFI’s own circumstances, the legal and regulatory environment under which it is operating and the particular facts of individual transactions. The information contained in these Guidelines is based on initial observations developed by the IIFM in conjunction with various discussion groups.
2. **GENERAL**

2.1. **General overview of the Islamic FX product**

Islamic Foreign Exchange Forward (IFX) essentially involves two dissimilar currencies. As per Shari‘ah (Islamic Law) the exchange of two dissimilar currencies / counter values must be spot or simultaneous (i.e. hand to hand) as it is considered to be Ribawi items (i.e., interest). In the IFX Forward transactions as they are being practiced in the current IFX market, the rate of exchange will be locked under the *Wa‘ad* principle on the date of the contract (i.e. the trade date) but the delivery of the two dissimilar currencies will be deferred to a future date (i.e. the settlement date). It is worth noting in this regard that Shari‘ah does not prohibit a promise to buy and sell currencies on one date with delivery to be made on another date because the proper contract only concludes on the day of delivery.

2.2. **Definition of Islamic Foreign Exchange (IFX)**

Islamic Foreign Exchange (IFX) is a *Wa‘ad* based contract that is designed as a hedging mechanism to minimize market participants’ exposure to market currency exchange rates which is volatile and fluctuating.

2.3. **Wa‘ad and its applications in contemporary Islamic financial transactions.**

2.3.1. **Definition of Wa‘ad (Promise/Undertaking).**

*Wa‘ad* is technically defined by scholars as: An expression of intent by the person who gives a promise to do or deliver something good in the future. *Wa‘ad* is considered to be unilateral in nature, because it occurs when only a party gives a promise to the other party that he will perform a certain action in the future.

2.3.2. **Permissibility of Wa‘ad in Shari‘ah.**

In general, a *Wa‘ad* or a promise to perform a lawful/ permissible (*Halal*) act in the future is allowed under the Shari‘ah principles. Whereas, there is a consensus among the Muslim scholars that it is unlawful/ impermissible (*Haram*) to make a promise to do something prohibited under the Shari‘ah principles. This includes making a promise without any intention of fulfilling it etc.

2.3.3. **Honouring/Fulfillment of Wa‘ad**

Muslim scholars agreed that it is obligatory to fulfill a promise made to Allah (God) Almighty in a form of a vow (nadhr/nazr), such as a promise to give charity or fast etc. However, they differed on a promise to do something permissible as to whether its fulfillment is *Wajib* (i.e., obligatory) or *Mustahabb* (i.e., recommended), and whether it is only *Mulzim Diyantan* (i.e., religiously binding) or also *Mulzim Qada’an* (i.e., legally binding) and therefore, enforceable in a court of law.

According to the Maliki school of thought honouring/ fulfillment of a *Wa‘ad* is obligatory and therefore, it is religiously and legally binding and enforceable in a court of law, especially, if the promise is attached to a cause and the promisee has acted upon the cause of the promise. This view is favoured by many contemporary
scholars. There are several resolutions issued on the bindingness and enforceability of Wa’ad among them:

- **OIC Fiqh Academy:** Resolution N. 40-41 (2/5 & 3/5) Concerning Discharging Of Promise And Murabaha For The Orderer Of Purchase.

The Council of the Islamic Fiqh Academy, in its Fifth session, in Kuwait-City (State of Kuwait), from 1st to 6th Jumada al-Oula 1409 H (10 to 15 December 1988) resolves:

**Quote:** “According to Shari'a, a promise (made unilaterally by the purchase orderer or the seller), is morally binding on the promisor, unless there is a valid excuse. It is however legally binding if made conditional upon the fulfillment of an obligation, and the promisee has already incurred expenses on the basis of such a promise. The binding nature of the promise means that it should be either fulfilled or a compensation be paid for damages caused due to the unjustifiable non fulfilling of the promise.”

- **AAOIFI:** Shari’ah Standard (Bilateral promise to purchase and sell currencies) Quote:

“A bilateral promise to purchase and sell currencies is forbidden if the promise is binding, even for the purpose of hedging against currency devaluation risk. However, a promise from one party is permissible even if the promise is binding” (AAOIFI: Shari’ah Standard No. 1: Trading in Currencies).

**2.3.4. Use of Wa‘ad in the Islamic FX forward to comply with Shari’ah requirements**

The Islamic FX forward structures are based on binding Wa‘ad which requires a party (i.e., the promisor) to promise to buy the relevant currency for settlement on a forward value date at the rate and amount agreed today.

*Wa‘ad* is used in this structure in order to comply with Shari’ah requirements that prohibit the deferment of any counter values in currency trading. As mentioned earlier, Shari‘ah does not prohibit a promise to buy and sell currencies on one date with delivery to be made on another date because the proper contract only concludes on the day of delivery. In other words, the actual currency trading only takes place on the value date, not at the dealing date, and therefore, no Riba issue arises because a mere Wa‘ad is not a contract.

**2.3.5. Bilateral Wa‘ad/promise to purchase and sell currencies**

**AAOIFI:** Shari’ah Standard (Bilateral promise to purchase and sell currencies) Quote:

“A bilateral promise to purchase and sell currencies is forbidden if the promise is binding, even for the purpose of hedging against currency devaluation risk...........” (AAOIFI: Shari‘ah Standard No. 1: Trading in Currencies).
2.3.6. Two unilateral independent Wa‘ad (Wa’ ‘adan)

In order to differentiate between two unilateral independent Wa‘ad and the bilateral Muwa‘adah the contemporary scholars have introduced the new term, namely Wa’ ‘adan, to avoid two promises becoming a binding Muwa‘adah, which is not allowed by many scholars.

Wa’ ‘adan is defined as: Two unilateral independent Wa‘ad / promises, given by one party to another, that are not interrelated, and their application depends on two different conditions. (Both promises are independent/ not interrelated and the application of the two promises depends on two different conditions that will eventually lead to the exclusive execution of one binding Wa‘ad/promise in the future).

2.3.7. The Difference between Wa’ ‘adan and Single Wa‘ad

The main difference between the two unilateral independent Wa‘ad and the Single Wa‘ad, is based on the number of parties giving the promises. In the two unilateral independent Wa‘ad there are two parties giving two promises that have different conditions, whereby in the Single Wa‘ad only one party gives the promise. However, both are similar in a sense that only one Wa‘ad will be ultimately exercised in both two unilateral independent Wa‘ad or Wa’ ‘adan and the Single Wa‘ad.

2.4. Commonly used structures for the Shari‘ah compliant IFX contracts

There are two structures which are commonly used in the market for the Shari‘ah compliant IFX hedging arrangements namely:

- Two Unilateral Independent Wa‘ad Structure.
- Single Binding Wa‘ad Structure.

  - **Under the two unilateral independent Wa‘ad structure**, each party to the agreement unilaterally will give an independent Wa‘ad (promise/undertaking) to exchange one currency against another currency, as the case may be, on a future date at a specified amount. Each Wa‘ad will contain a different set of conditions such that only one of the Wa‘ad can be exercised on the settlement date with no further obligations arising under the other Wa‘ad (promise/undertaking).

  - **Under the single binding Wa‘ad** structure a binding Wa‘ad (promise/undertaking) will be applied whereby the party who promised to buy or sell, as the case may be, is obliged to fulfill that promise. It is worth to note in this regard that as per Shari‘ah (i.e., Islamic Law), a binding Wa‘ad from only one party is not deemed as a contract. Thus, this can make the process of the Islamic FX contracts as they are currently being applied in the market acceptable from a Shari‘ah perspective.
2.5. The fundamental differences between two unilateral independent and single binding Wa’ad structures

The main difference between the two unilateral independent Wa’ad based structure and the single binding Wa’ad based structure is as follows:

Under the two unilateral independent Wa’ad based structure, each party to the agreement unilaterally gives an independent Wa’ad (promise/ undertaking) to exchange one currency against another currency on a future date at a specified amount. Each Wa’ad as explained earlier, will contain a different set of conditions such that only one of the undertakings can be exercised on the settlement date with no further obligations arising under the other promise.

The single binding Wa’ad based structure involves one party who is looking for a hedge to purchase a specified currency at a future date based on the rate determined today, providing a binding Wa’ad (promise / undertaking) to purchase such currency. In this transaction the party who is looking for a hedge will identify his requirement, for instance, he has surplus funds denominated in currency (a) (for example USD) and wishes to invest in currency (b) (for example Euro), but he is concerned that the exchange rate fluctuation of currency (a) and currency (b) may expose him to cash flow uncertainty and therefore wishes to mitigate this risk.
3. IIFM IFX PRODUCT OVERVIEW

3.1. IIFM & ISDA published templates

ISDA and IIFM have published template master terms and conditions (the "IFX Master Terms and Conditions") to be used to document Islamic Foreign Exchange Forwards or Wiqayah Min Tagailub As’aar Assarf ("IFX Forward") under the ISDA/IIFM Tahawwut (Hedging) Master Agreement (the "TMA"). This explanatory guidance memorandum explains the Islamic structures used, sets out the key features of these templates and contains other useful information.

Two sets of IFX Forward standard templates have been published, as follows:

- **Set 1.** IFX Forward templates that are based on the two unilateral independent *Wa’ad* structure (the "Two Wa’ad Structure"); and
- **Set 2.** IFX Forward templates based on the single binding *Wa’ad* structure (the "Single Wa’ad Structure").

**ISDA/IIFM Tahawwut (Hedging) Master Agreement (TMA)**

The TMA is a master agreement that contains the general terms and conditions agreed between the parties and under which parties may enter into "Transactions" and/or "DFT Terms Agreements" relating to "Designated Future transactions".

The TMA draws a distinction between "Transactions" that have been entered into between the parties and "Designated Future transactions" that will or may be entered into between the parties in the future. This is an important distinction which is key to the different close-out mechanisms which apply to these two types of arrangement.

The terms of a Designated Future transaction are provided for in a DFT Terms Agreement, which is evidenced by a "DFT Terms confirmation". The TMA uses upper and lower case "Transactions", "transactions", "Confirmations" and "confirmations" to help distinguish between the two types of arrangement and the manner in which they are documented. The IFX Master Terms and Conditions of an IFX Forward, as supplemented by the relevant *Wa’ad* (Undertaking) given by the relevant party, constitutes a DFT Terms confirmation for the purpose of the TMA. The IFX Master Terms and Conditions only need to be executed by the parties once at the outset of the trading relationship or at the time of entering into the first IFX Forward transaction, but the relevant Undertaking(s) relating to the IFX Forward (which will supplement the IFX Master Terms and Conditions) will need to be executed for each IFX Forward transaction.

The terms of the Transaction (i.e. the actual sale and purchase of the relevant currencies) are evidenced by a "Confirmation". The Offer and Acceptance (a form of which is annexed to the IFX Master Terms and Conditions) once executed, constitutes a Confirmation for the purposes of the TMA.

A failure by the Buyer to accept the Seller’s Offer in accordance with the provisions of the IFX Master Terms and Conditions constitutes a failure by the Buyer to enter
into a Designated Future transaction when required to do so in accordance with a DFT Terms Agreement which is an Event of Default under the TMA.

3.2. **IFX Product Purpose**

An IFX Forward enables market participants to hedge their exposure to fluctuating currency exchange rates. Parties’ can lock in the exchange rate for the purchase or sale of a currency on a future date. For example, where a party has an investment in one jurisdiction in relation to which it has obtained funding denominated in the currency of that jurisdiction, but the party accounts in the currency of its home jurisdiction, the IFX Forward provides it with the potential to hedge its foreign currency requirements into the currency of its home jurisdiction.

3.3. **IFX Forward templates are based on Wa‘ad (promise/undertaking)**

The IFX Forward templates are based on the Wa‘ad structure. A Wa‘ad in this case is an undertaking / promise made by one party (the Buyer) to the other party (the Seller) that, if required by the Seller (usually called exercise of the Wa‘ad or undertaking), the Buyer will fulfil its promise, in this case, to enter into a transaction under which it will buy from the Seller one currency in exchange for another currency on the relevant settlement date.

The Wa‘ad will need to be entered into with respect to each IFX Forward transaction. For the two unilateral independent Wa‘ad structure, each party needs to execute a Wa‘ad. For the single binding Wa‘ad Structure, only one party needs to execute a Wa‘ad.

If and when the relevant Wa‘ad is exercised by the Seller on the relevant Exercise Date (by the Seller sending an Exercise Notice), the Buyer is required to purchase a specified amount of one currency in exchange for a specified amount of another currency. The Buyer and Seller will confirm the terms of such sale by executing an Offer and Acceptance.

The mechanics of the sale and purchase are set out in Part 3 of each template IFX Master Terms and Conditions. Forms of Undertaking(s), Exercise Notice and Offer and Acceptance are annexed to the IFX Master Terms and Conditions.

3.4. **Product Description**

3.4.1. **Two Unilateral Independent Wa‘ad Structure**

The two unilateral independent Wa‘ad structure provides for each party to grant a Wa‘ad (Undertaking) to the other party. It is envisaged that under each Undertaking one party (the Buyer of the relevant currency) gives a Wa‘ad to the other party (the Seller of the relevant currency) under which the Seller may, if the specified condition (the "Exercise Condition") set out in the Undertaking is satisfied, exercise the Buyer’s Undertaking requiring the Buyer to purchase from the Seller one currency in exchange for another currency.

Each Undertaking will be exercisable only if the relevant Exercise Condition is satisfied. The respective Exercise Conditions are such that, if the Exercise Condition under one Undertaking is satisfied, then the Exercise Condition under the other
Undertaking will not be satisfied, so that only one of the Buyer’s or Seller’s Undertaking will be exercisable.

The Exercise Condition in respect of Party A’s Undertaking is satisfied in respect of the Exercise Date if the Spot Rate on the Exercise Date is \textit{less than or equal} to the Forward Rate. The Exercise Condition in respect of Party B’s Undertaking is satisfied in respect of the Exercise Date if the Forward Rate is \textit{greater than} the Spot Rate on the Exercise Date.

The IFX Forward templates relating to the two \textit{Wa’ad} structure comprise of the IFX Master Terms and Conditions which need to be executed by the parties only once at the outset of the trading relationship or at the time of the first IFX Forward transaction. At the time of entering into each IFX Forward transaction, each party needs to grant a \textit{Wa’ad} (Undertaking) to the other party. Forms of Undertakings for each party are contained in Annexes 1 and 2 to the IFX Master Terms and Conditions. There is a \textit{Shari’ah} preference for the \textit{Wa’ads} (Undertakings) of one party to be clear and distinct from, and not combined with, that of the other. The diagram set out at paragraph 3.5 below illustrates the two unilateral independent \textit{Wa’ad} based structure.

\textbf{Explanation of documentation process}

1. The parties execute the IFX Master Terms and Conditions only once at the outset of the trading relationship or at the time of the first IFX Forward transaction.

2. In respect of an IFX Forward transaction, Party A, the Undertaking provider, will send an Undertaking in the “Form Of Party A’s Undertaking” set out at Annex 1 to the IFX Master Terms and Conditions to Party B so that on the relevant Settlement Date specified in the Undertaking, it will purchase the relevant currency amount from Party B, on the terms and subject to the conditions of the DFT Terms confirmation only if the Spot Rate is \textit{less than or equal} to the Forward Rate on the Exercise Date. Party B will acknowledge the Undertaking.

3. In respect of an IFX Forward transaction, Party B, the Undertaking provider, will also send an Undertaking in the “Form Of Party B’s Undertaking” set out at Annex 3 to the IFX Master Terms and Conditions to Party A so that on the relevant Settlement Date specified in the Undertaking, it will purchase the relevant currency amount from Party B, on the terms and subject to the conditions of the DFT Terms confirmation only if the Forward Rate is \textit{greater than} the Spot Rate on the Exercise Date. Party A will acknowledge the Undertaking.

4. The Seller being the relevant Undertaking recipient which could be either party, will send the Exercise Notice in the “Form Of Exercise Notice” set out at Annex 2 to the IFX Master Terms and Conditions to the Buyer exercising the Buyer’s Undertaking requesting the Buyer, on the Settlement Date, to purchase from the Seller the First Currency Amount of the First Currency for the Second Currency Amount of the Second Currency on the specified terms.
5. The Offer and Acceptance will also be sent by the Seller, the relevant Undertaking recipient to the Buyer (who will countersign the Offer and Acceptance). The purpose of the form of the Offer and Acceptance is to confirm the terms and conditions of the sale transaction entered into between the parties, after the Seller has delivered to the Buyer an Exercise Notice.

As Only one *Wa’ad* can be exercised on the Exercise Date.

### 3.4.2. Single Binding *Wa’ad* Structure

The Single Binding *Wa’ad* Structure envisages that under the Undertaking one party (the Buyer of the relevant currency) gives a *Wa’ad* to the other party (the Seller of the relevant currency) under which the Seller may exercise the Buyer’s *Wa’ad* requiring the Buyer to purchase from the Seller one currency in exchange for another currency.

The IFX Forward templates relating to the Single Binding *Wa’ad* Structure comprise of the IFX Master Terms and Conditions which need to be executed by the parties only once at the outset of the trading relationship or at the time of the first IFX Forward transaction. At the time of entering into each IFX Forward transaction, the Buyer needs to grant a *Wa’ad* (Undertaking) to the Seller. A form of the Undertaking is contained in Annex 1 to the IFX Master Terms and Conditions. The diagram set out at paragraph 3.5 below illustrates the single *Wa’ad* based structure:

**Explanation of documentation process:**

1. **The parties execute the IFX Master Terms and Conditions only once at the outset of the trading relationship or at the time of the first IFX Forward transaction**

2. **Buyer's Undertaking.** In respect of an IFX Forward transaction, the Buyer will deliver to the Seller a Buyer's Undertaking to purchase from the Seller on the Settlement Date a specified amount of the First Currency by payment of the specified amount of the Second Currency on the relevant Settlement Date.

3. **Exercise of Buyer’s Undertaking and Seller's Offer.** In respect of an IFX Forward transaction, the Seller, as the recipient of the Buyer's Undertaking, will be entitled to deliver to the Buyer, on or prior to the Exercise Date, an Exercise Notice for the *Wa’ad* (Undertaking) the Seller received from the Buyer to purchase from the Seller the First Currency.

   The Exercise Notice shall be accompanied by two copies of an Offer and Acceptance constituting an offer by the Seller to the Buyer to enter into the relevant IFX Sale Transaction.

4. **Buyer's Acceptance.** Following the delivery to the Buyer by the Seller of the Exercise Notice with respect to the Exercise Date, together with two copies of the duly completed Offer and Acceptance executed by the Seller, the Buyer shall accept such offer either orally by telephone or in writing via email, or any other recognized means or by countersigning such Offer and Acceptance and returning one such original to the Seller on the same day as that on which the Exercise Notice became effective. If the Buyer accepts such offer by
telephone or via email, then such acceptance shall be subsequently confirmed by returning to the Seller a duly signed copy of the Offer and Acceptance form, although any failure to do so shall not invalidate such acceptance.

3.5. Documentation architecture for the Two Wa‘ad Structure and the Single Wa‘ad Structure

Diagrams illustrating the documentation architecture for the Two Wa‘ad Structure and Single Wa‘ad Structure are set out below.

Two Unilateral Independent Wa‘ad Structure
documentation architecture

*TThe beneficiary of the relevant Undertaking will acknowledge the Undertaking.
*There will only be one Exercise Notice and one Offer and Acceptance under the relevant Wa‘ad (Undertaking) that is exercised (i.e. the Wa‘ad under which the Exercise Condition is satisfied)
3.6. Designated future transactions (DFT)

Pursuant to the TMA, the parties may from time to time agree (the documents and other confirming evidence exchanged between the parties or otherwise effective for the purpose of confirming or evidencing any such agreement being a "DFT Terms confirmation" and each such agreement being a "DFT Terms Agreement") the terms of further transactions in each case being either (i) a transaction which, by such DFT Terms Agreement, the parties agree to enter into between them in the future under the TMA or (ii) a transaction which, by such DFT Terms Agreement, one party (the first party) undertakes to the other (the second party) to enter into under the TMA at the election of the second party at a future date (all of such further transactions being "Designated Future transactions"). Except as is expressly provided in the TMA, Designated Future transactions shall not constitute Transactions for the purposes of the TMA unless and until subsequently entered into, and when entered into they shall constitute Transactions, shall be confirmed by way of a Confirmation and shall cease to be Designated Future transactions. The TMA draws a distinction between "Transactions" that have been entered into between the parties and "Designated Future transactions" that will or may be entered into between the parties in the future. This is an important distinction which is key to the different close-out mechanisms which apply to these two types of arrangement.

The IFX Master Terms and Conditions of an IFX Forward, as supplemented by the relevant Undertaking given by the relevant party, constitutes a DFT Terms confirmation confirming the DFT Terms Agreement for the purposes of the TMA.
The IFX Forward transaction evidenced by the relevant Undertaking(s) constitutes a Designated Future transaction for the purposes of the TMA. The IFX Master Terms and Conditions only need to be executed by the parties at the outset of the trading relationship or at the time of the first IFX Forward transaction, but the relevant Undertaking(s) related to the IFX Forward will need to be executed for each IFX Forward transaction.

The terms of a Transaction are evidenced by a "Confirmation". The Offer and Acceptance (a form of which is annexed to the IFX Master Terms and Conditions) once executed, constitute a Confirmation for the purposes of the TMA. The sale and purchase of the relevant currencies constitutes a Transaction for the purpose of the TMA.

3.7. IFX Forward Key Terms

Set out below are some of the key terms relating to an IFX Forward that need to be specified in the relevant Undertaking(s) relating to the IFX Forward.

**Buyer** is the party that undertakes to purchase the First Currency from the Seller for the Second Currency.

**Seller** is the party that will sell the First Currency for the Second Currency to the Buyer.

**Trade Date** is the date on which the parties enter into the relevant IFX Forward transaction.

**Exercise Date** is the date on which the relevant Wa’ad (Undertaking) can be exercised by the Seller delivering an Exercise Notice to the Buyer.

**Settlement Date** is the date on which the Buyer shall transfer to the Seller the Second Currency Amount of the Second Currency and the Seller shall transfer to the Buyer the First Currency Amount of the First Currency.

**First Currency** and **First Currency Amount** is the currency and amount to be purchased by the Buyer. In the Two Wa’ad Structure, this would be the "Second Currency" and "Second Currency Amount" in the related Undertaking.

**Second Currency** and **Second Currency Amount** is the currency and amount to be delivered to the Seller. In the Two Wa’ad Structure, this would be the "First Currency" and "First Currency Amount" in the related Undertaking.

**Forward Rate** is the currency exchange rate to be specified in the relevant Undertaking(s). The Forward Rate in each Undertaking should be expressed as an amount of the Second Currency per one unit of the First Currency. The Forward Rate is relevant to determining whether the Exercise Condition has been satisfied. The Exercise Condition in respect of Party A’s Undertaking is satisfied in respect of the Exercise Date if the Spot Rate on the Exercise Date is less than or equal to the Forward Rate. The Exercise Condition in respect of Party B’s Undertaking is satisfied in respect of the Exercise Date if the Forward Rate is greater than the Spot Rate on the Exercise Date. The Forward Rate (and Exercise Condition) is only relevant to the Two Wa’ad Structure.
The Forward Rate (and Exercise Condition) are not relevant to or used in the IFX Forward templates for the Single Wa’ad Structure.

3.8. **Key Features of the IFX Master Terms and Conditions**

**Transaction terms**

The IFX Master Terms and Conditions only need to be executed by the parties at the outset of the trading relationship or at the time of the First IFX Forward transaction. The relevant Undertaking(s) relating to the IFX Forward will need to be executed for each IFX Forward transaction. Template Undertaking(s) are annexed to the IFX Master Terms and Conditions and contain line items for specific agreed terms to be completed on the Trade Date (as detailed in paragraph 3.7 above).

**Annexed pro-forma documents**

Form(s) of Undertaking(s) are included in Annex 1 (and Annex 2 for the Two Wa’ad Structure) of the IFX Master Terms and Conditions. The form of Undertaking(s) is intended to be extracted and completed by the parties on the Trade Date. For the Two Wa’ad Structure, each party will execute a separate Undertaking. For the Single Wa’ad Structure, only one party will execute an Undertaking.

A form of Exercise Notice is included in Annex 3 of the IFX Master Terms and Conditions for the Two Wa’ad Structure and Annex 2 of the IFX Master Terms and Conditions for the Single Wa’ad Structure. The form of Exercise Notice is intended to be extracted, completed and used by the Seller when it wishes to exercise the Buyer's Undertaking on the Exercise Date.

A form of Offer and Acceptance (i.e. a "Confirmation" for the purposes of the TMA) is included in Annex 4 of the IFX Master Terms and Conditions for the Two Wa’ad Structure and Annex 3 of the IFX Master Terms and Conditions for the Single Wa’ad Structure. This form is intended to be extracted, completed and used to document entry into the relevant sale and purchase of currencies (i.e. a "Transaction" for the purposes of the TMA).

Once completed and executed, the Offer and Acceptance will constitute a Confirmation for the purposes of the TMA.

**Footnote guidance**

Extensive footnotes are included throughout the template IFX Master Terms and Conditions (including the annexes thereto) to provide guidance to the parties but these do not form part of the terms of the contract between the parties.

As a practical and drafting matter, a new clean version of the relevant template, without footnotes, will need to be created before the parties agree and finalise the relevant terms.

**Execution as a Deed**

In order to comply with requirements under English law for unilateral undertakings, the usual practice in the Islamic finance market is that a Wa’ad (Undertaking) is
evidenced or confirmed as a deed and, therefore, the IFX Forward templates provide for the Buyer to enter into the relevant Undertaking as a deed. The parties will need to satisfy themselves as to the correct form of words to be used in the place designated for signature by the Buyer to ensure that the relevant Undertaking is properly executed as a deed.
4. **IIFM SHARI‘AH BOARD GUIDELINES FOR THE USE OF THE IIFM IFX FORWARD PRODUCT**

While IIFM’s Shari‘ah Board has approved the IFX Forward templates after extensive consideration, it is always the responsibility of each of the parties entering into the IFX Forward to ensure that, to the extent that Shari‘ah compliance is relevant to its dealings and corporate governance, its use of the documents in the context of the transactions which it enters into satisfies its own Shari‘ah advisers that the relevant hedging transaction is Shari‘ah compliant and that the documents are suitable for, and are being used appropriately in, the context of that particular hedging transaction.

In order to assist market participants with regard to the IFX Master Terms and Conditions provided to market participants by IIFM and ISDA, the IIFM Shari‘ah Board members have provided the following guidelines regarding Shari‘ah compliance of this product:

1. IFX Forward transactions should be entered into only for the purpose of hedging actual risks of the relevant party.

2. The transactions/contracts should not be entered into for purposes of speculation.

3. No interest/Riba (whether called interest or an alternative name but which represents interest) is to be chargeable under an IFX Forward transaction.

4. The exchange of two dissimilar currencies/countervalues must be spot or simultaneous (i.e. hand to hand) taking into consideration the banking rulings allowed by Fiqh (jurisprudence) academies in respect of currency transactions.

5. The counter values of the same currency must be of equal amount, even if one of them is in paper money and the other is in coin of the same country, like a note of one pound for a coin of one pound.

6. The contract shall not contain any conditional option or deferment clause regarding the delivery of one or both counter values.

7. A bilateral promise to purchase and sell currencies is forbidden if the promise is binding, even for the purpose of hedging against currency devaluation risk. However, a promise from one party is permissible even if the promise is binding.

8. Under the two unilateral Wa‘ad based structure, each Wa‘ad should be **independent and separate** from the other and contingent on two different events.
ضوابط العمل بهذا المنتج

على المستخدمين المحتملين لهذه الوثيقة أن يضعوا في الاعتبار بأنه عند إبرام أو الدخول في هذه المعاملات أو الترتيلات التي تتعلق بالشروط والأحكام الرئيسية لاتفاقية الوعد بالصرف في المستقبل (وقائية من تقلب أسعار الصرف) القائم على هيكل وعدين منفصلين مختلفي المورد من طرفين وقائم على هيكل وعد ملزم من طرف واحد، فإن عليهم أولاً اتخاذ كافة الإجراءات للتأكد من أن المعاملات أو الترتيلات هذه متبقية مع أحكام ومبادئ الشريعة الإسلامية. وعلى المستخدمين الذين أرادوا إدخال تعديل أو إضافة على هذه الوثيقة اتخاذ كافة الإجراءات الائتمانية للإطمئنان بأن أي تعديل أو إضافة في المستند متبقية مع أحكام ومبادئ الشريعة الإسلامية.

من أجل مساعدة المشاركين في السوق فيما يتعلق بهذه الوثيقة "الشروط والأحكام الرئيسية لاتفاقية الوعد بالصرف في المستقبل (وقائية من تقلب أسعار الصرف) القائم على هيكل وعدين منفصلين مختلفي المورد من طرفين وقائم على هيكل وعد ملزم من طرف واحد، التي تقدمها السوق المالية الإسلامية الدولية للمشاركين في السوق، فقد قدمت الهيئة الشرعية للسوق المالية الإسلامية الدولية الضوابط التالية بشأن توافق هذا المنتج مع أحكام ومبادئ الشريعة الإسلامية:

(أ) لا تبرم هذه العقود إلا لغرض التحوط من المخاطر الحقيقية للطرف ذي العلاقة.
(ب) لا تبرم هذه العقود ولا يجوز استعمالها لأغراض المضاربات (المجازفة).
(ج) يجب أن يكون تبادل هيئة روية مهما كانت تسميتها ( أي سواء سميت فائدة/الربا أو باسم آخر ولن تكون فائدة/الربا) وذلك بموجب هذه المعاملة.
(د) يجب أن يكون تبادل هيئة روية غير المتماثلين فوقاً ( أي بدون) مع الأخذ بالإعتبار القيود المصرفية.
(ه) يجب أن يتم التماثل في البلدين اللذين هما من أجل واحد وللو كان أحدهما عملة ورقية والآخر عملة معدنية.
(و) لا يجوز أن يتضمن العقد على خيار شرط أو أجل تسلم أحد البلدين أو كليهما.
(ز) لا تجوز المواعدة في المتأخرة في المعاملة إذا كانت ملزمة للطرفين ولو كان ذلك لمعالجة مخاطر هبوط العملة.
(ح) إذا تم الاتفاقية على وعدين فيجب أن يكون كل واحد منهما منفصلا عن الآخر ومختلفه المورد.
5. OTHER MATTERS

5.1. These IIFM/ISDA IFX documents are for plain vanilla FX forwards only.

The current documents are for vanilla deliverable FX forwards only. IIFM will consider projects in the future for other IFX products if deemed necessary.

5.2. Use of a single Wa‘ad (undertaking) for a strip of unconditional IFX Forward transactions.

Strip of IFX Forward transactions - Parties may, if they wish, agree to sign a single Wa‘ad (undertaking) for a strip of IFX Forward transactions. If this is the case, relevant amendments will need to be made to the IFX Master Terms and Conditions (and the Annexes thereto) to cater for this (for example, the First Currency/First Currency Amount, Second Currency/Second Currency Amount, Spot Rate/Forward Rate and Exercise Dates/Settlement Dates would need to be separately specified for each separate strip of IFX Forward). This is subject to each strip of IFX Forward being permissible on its own from a Shari‘ah perspective. The party requiring Shari‘ah compliance should seek its Shari‘ah board approval if it decides to use a single undertaking for a strip of unconditional IFX Forward transactions.

5.3. Each Wa‘ad should be executed as a deed.

Given that each Wa‘ad is documented as a separate undertaking and that each Wa‘ad is a unilateral undertaking from one party to another, it is advisable from an English law perspective that these are executed as deeds so that there is no issue as to whether or not there has been sufficient consideration provided by the parties. This is standard practice in Islamic transactions utilising the dual Wa‘ad structure. For the two Wa‘ad structure, it is recommended that institutions ensure that the two Wa‘ads are executed and released at the same time.

5.4. Is it possible to have one undertaking to purchase currency A and other undertaking to sell currency A under the documents?

The decision to have the approach of having an undertaking to purchase from each party was taken given market participant’s preference to minimise/simplify the documents that need to be executed for each trade. If we were to have an undertaking to purchase and an undertaking to sell, we would need to have two separate sets of master terms and conditions with associated undertakings which is something market participants did not prefer to have.

5.5. Given the Wa‘ad should be managed by each institution when completing the IFX documents what is the reason for not specifying which type of institution will be Party A or Party B?

The reason is that the IFX Forward templates are market standard documents to be used by a variety of institutions and as such they will not pre-specify which type of institution will be Party A or Party B. This is something that needs to be managed by each institution when completing the confirmations.
5.6. Early unwind under the ISDA/IIFM Tahawwut Master Agreement contemplates entering into a commodity transaction. Typically early unwinds for FX transactions are by way of acceleration of currency promise. Should we have an alternate unwind mechanic for IFX forwards in line with market practice?

Various transactions will be entered into under the Tahawwut Master Agreement and the idea is to have a single net close-out amount so there needs to be a single close-out mechanism across all transactions. The approach of having alternate unwind mechanics only works under bespoke standalone FX documentation but not for a multi product master agreement.

5.7. Can the Exercise Date be specified in the IFX Master Terms and Conditions instead of the Undertaking(s)?

This is transaction specific so it needs to be specified in the relevant Undertaking. The Exercise Date is the date on which the seller/promissee is entitled to exercise its right to require performance under the undertaking. This date, therefore, relates to settlement and will be a date specified at the time of entering into each transaction and will differ for each transaction.

5.8. What is the rationale of the Exercise Notice in the IFX Forward documents (can Offer and Acceptance suffice instead of having the Exercise Notice)?

It is a Shari’ah requirement to have an exercise notice whereby the beneficiary of the Wa‘ad/undertaking can choose whether to exercise or not – without this, exercise would be automatic. According to AAOIFI Standard No. 8: Murabaha for a Purchase-Orderer: “A bilateral promise between the customer and the institution is permissible only if there is an option to cancel the promise which may be exercised either by both promisors or by either one of them”.

5.9. What is the rationale for the Undertakings to be executed as deeds?

Due to issues under English law as to whether sufficient consideration has been provided under a unilateral Wa‘ad (Undertaking) to form a contract under English law, each Wa‘ad (Undertaking) should be executed as a deed. Relevant execution blocks for deeds have been provided in the forms of Undertakings to the IFX Master Terms and Conditions.
6. **APPENDIX 1 – ILLUSTRATIVE EXAMPLE IN RELATION TO THE TWO UNILATERAL **

**WA’AD STRUCTURE**

**Wa’ad 1**
First Currency = GBP  
Second Currency = USD

<table>
<thead>
<tr>
<th>Bank (Buyer)</th>
<th>Customer (Seller)</th>
</tr>
</thead>
<tbody>
<tr>
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</tbody>
</table>

Promises to buy GBP 1 million at the Forward Rate of 1.51 if USD/GBP Spot Rate ≤ Forward Rate

**Wa’ad 2**
First Currency = USD  
Second Currency = GBP

<table>
<thead>
<tr>
<th>Customer (Buyer)</th>
<th>Bank (Seller)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Promises to buy USD 1.51 million at the Forward Rate of 0.66 if Forward Rate > GBP/USD Spot Rate

Scenario 1: on the Exercise Date if USD/GBP Spot Rate is ≤ 1.51, the Customer exercises its rights under **Wa’ad 1**, so that on the Settlement Date, the Bank buys GBP 1 million in exchange for USD 1.51 million.

Scenario 2: on the Exercise Date, if USD/GBP Spot Rate is > 1.51 (i.e. Forward Rate of 0.66 > GBP/USD Spot Rate), the Bank exercises its rights under **Wa’ad 2**, so that on the Settlement Date, the Customer buys USD 1.51 million for GBP 1 million.
On the Exercise Date, the Bank exercises its rights under the *Wa’ad*, so that the Customer buys GBP 1 million in exchange for USD 1.51 million. Although for *Shari’ah* related reasons the Bank is not strictly under an obligation to exercise its rights under the *Wa’ad*, given that this is an IFX Forward product the expectation is that it would do so.