AAOIFI Financial Accounting Standard 38

Wa’ad, Khiyar and Tahawwut

Contents

AAOIFI Financial Accounting Standard (FAS) 38 "Wa'ad, Khiyar and Tahawwut" is set out in paragraphs 01-35. All the paragraphs have equal authority. This standard should be read in the context of its objective and the Conceptual Framework for Financial Reporting as endorsed by AAOIFI.

All AAOIFI FASs shall be read in conjunction with the definitions, Shari'ah principles and rules key considerations provided by AAOIFI Shari'ah Standards (SS) in respect of such products and matters. This standard in particular, shall be read in line with SS 25 "Combination of contracts", SS 45 "Protection of capital and investments", SS 49 "Unilateral and bilateral promise", SS 52 "Options to reconsider (cooling-off options, either-or options, and options to revoke due to non-payment), SS 53 "Arboun (earnest money)", and SS 54 "Revocation of contracts by exercise of a cooling-off option".

Preface

PR1 With the growth of Islamic finance, there are newer transactions becoming common in the market, including several that are based on Wa'ad (promise / undertaking) and Khiyar (option). In addition, risk management practices need, at times, Shari'ah compliant Tahawwut (hedging) transactions. Moreover, it is common to use such products as ancillary to various Islamic finance products.

PR2 The objective of this standard is to set out the accounting principles for measurement, recognition, and disclosure of Wa'ad, Khiyar and Tahawwut transactions that are carried out by Islamic financial institutions (the institutions).

PR3 Wa'ad and Khiyar are used by institutions in various forms. Some are ancillary to other transactions, whereas in certain other transactions these are used as primary products. This standard intends to provide accounting principles for both of these situations, as well as the Tahawwut transactions which are normally based on Wa'ad or Khiyar, or a series or combination thereof. These may, as well, take the form of products like a series of commodity Murabaha transactions.

Introduction

Overview

IN1 This Financial Accounting Standard (FAS) 38 "Wa'ad, Khiyar and Tahawwut" prescribes the accounting and reporting principles and requirements for Wa'ad (promise), Khiyar (option) and Tahawwut (hedging) arrangements for the institutions.

IN2 Many products e.g., Murabaha, Ijarah, diminishing Musharaka etc. offered by the institutions combine the application of Wa'ad or Khiyar in one form or another. Ancillary Wa'ad or Khiyar, in line with this standard, is such Wa'ad or Khiyar associated with a Shari'ah compliant arrangement by relation to its structure which does not give rise to any asset or liability unless it has turned into an onerous contract or commitment.

IN3 Product Wa'ad or Khiyar, on the other hand, is a stand-alone Shari'ah compliant arrangement which is used either as a normal product or, at times, for the purpose of Tahawwut. It may take the form of a single transaction or a series or combination thereof and may convert into a future transaction or series of transactions, in line with Shari'ah principles and rules. Such transactions give rise to an asset or a liability for the parties, subject to the conditions specified in this standard.

IN4 Hedge accounting is a method of accounting where an adjustment to, or movement / change in the fair value of an instrument and its corresponding hedged item(s) is recognised as a single adjustment / change, rather than treating this individually as distinct and separate. The institutions and their customers, at times, have to resort to Shari'ah compliant Tahawwut arrangements for hedging their volatile positions. Hedge accounting attempts to reduce the volatility created by the repeated adjustment to the instrument's value, known as fair value accounting or mark to market. This standard also addresses this aspect of accounting.

Rationale for issuing this standard

IN5 AAOIFI Accounting Board (AAB / the board) included the Wa'ad and Khiyar project in its work plan as these are integral parts of many Shari'ah compliant products, and their use is increasing as a stand-alone product with the development of the industry.

IN6 The board observed that clear guidance is required to ensure that accounting treatments of Wa'ad and Khiyar are similar and comparable between jurisdictions and entities.

IN7 Tahawwut arrangements are also included in the scope of this standard as these are increasingly used and accepted as a method to manage market risks by the institutions.

AAOIFI Financial Accounting Standard 38
Wa'ad, Khiyar and Tahawwut

Objective of the standard

1. The objective of this standard is to prescribe the accounting and reporting principles for recognition, measurement and disclosures in relation to Shari'ah compliant Wa'ad (promise), Khiyar (option) and Tahawwut (hedging) arrangements for Islamic financial institutions (the institutions).

Scope

2. This standard applies to accounting and financial reporting for all transactions involving Wa'ad, Khiyar or Tahawwut arrangements carried out under Shari'ah principles and rules.

Definitions

3. For the purpose of interpreting and applying this standard, the following short definitions are relevant:

    a. Arboun – is the amount paid by the buyer to the seller in a sale transaction at the time of contract as a security-cum-advance payment against the sales price. In line with contractual terms and the applicable Shari'ah principles and rules, it may be forfeited by the seller in case of revocation of purchase by the buyer during an agreed period of time;

    b. Control – an institution controls an asset or business, when it has substantially all risks and rewards incidental to ownership of such asset or business, duly meeting both of the following conditions:

        i. it is directly exposed to, or has rights to, variable returns (negative or positive, respectively) from its involvement with such assets or business; and

        ii. it has the ability to affect those returns through its power over the assets or business;

    c. Fair value – is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date;

    d. Hamish Jiddiyyah – is the amount deposited as a security for execution / fulfillment of a contract, or promise, or completion of a transaction by one of the parties to the other. [Explanation: The amount that can be forfeited therefrom is only the actual damages incurred due to a party's refusal to conclude the contract of sale. If Hamish Jiddiyyah falls short of the amount of actual damage, the affected party can have recourse to the other for any remaining amount. Hamish Jiddiyyah for a sale transaction cannot be used throughout the term of the contract, as it only relates to the pre-contracting period and until the conclusion / consummation of the contract];

    e. Khiyar (option) – is an option (expressed or implied) that is contained within a sale, Ijarah or other contract, allowing one party to unilaterally nullify or revoke the contract or to unilaterally amend the contract in a manner that the subject matter is materially changed;

f. Onerous contract or commitment – is a contract or commitment, respectively, in which the unavoidable costs of meeting the obligations under the contract or commitment, respectively, exceed the economic benefits expected to be received under it;

g. Promisor – is the party showing willingness to act on a particular subject matter;

h. Promisee – is the party to whom willingness to act on a particular subject matter has been shown by the promisor. The promisee may incur any cost by reason of the promise made by the promisor;

i. Tahawwut (hedging) arrangement – is a mechanism to mitigate the risk of unfavorable future fair value changes or cash flow differentials by way of entering into a Wa'ad or Khiyar arrangement (for a stipulated period of time) or a series thereof;

j. Wa'ad (promise) – is a unilateral undertaking (constructive obligation) assumed by a party to the arrangement. The unilateral promise is understood to be binding in Shari'ah on the individual who makes it, unless a legitimate excuse under Shari'ah arises and prevents its fulfillment. Wa'ad may be classified as:

    i. binding Wa'ad (promise) – is a Wa'ad which becomes binding on the promisor by virtue of juristic rules if it is pending on a cause and the promisee has incurred costs by reason of the promise, or by virtue of the promisor expressly making the same binding on itself; and

    ii. non-binding Wa'ad (promise) – is a Wa'ad other than a binding promise.

Types and classification of Wa'ad, Khiyar and Tahawwut arrangements

4. Wa'ad and Khiyar arrangements may be categorized into the following types:

    a. ancillary Wa'ad or Khiyar – where the Wa'ad or Khiyar is associated with a Shari'ah compliant arrangement, and is related to the structure of the transaction, e.g., a promise by the purchase orderer (potential buyer) attached to a Murabaha transaction, or a promise to purchase after the end of the Ijarah term in an Ijarah Muntahia Bittamleek transaction, or the option of seeing (i.e., inspecting) in a sale transaction; and

    b. product Wa'ad or Khiyar – where the Wa'ad or Khiyar is used as a stand-alone Shari'ah compliant arrangement in itself e.g., foreign exchange forward promise or an option of cancellation of a sale with Arboun. This may, inter-alia, take the following forms, in line with Shari'ah principles and rules:

        i. a promise to make a sale contract, or a promise to enter into an Ijarah transaction;

        ii. an option for revocation of sale contract – with or without Arboun;

        iii. a Shari'ah compliant alternative to re-purchase option (RePO) transaction – through a permissible Wa'ad or Khiyar[1]; and

[1] Kindly refer to SS 58 "Repurchase Agreements"

iv. a Tahawwut arrangement – whereby a Wa’ad or Khiyar, or a series of Wa’ad and Khiyar is used for a hedging arrangement.

Accounting for ancillary Wa’ad or Khiyar

Recognition and measurement

5. An ancillary Wa’ad or Khiyar by itself does not give rise to any asset or liability.

6. An institution shall, at the end of each financial reporting period, assess whether any of the ancillary Wa’ad or Khiyar, in either capacity of a promisor or promisee, has turned into an onerous contract or commitment for the institution.

7. An institution shall account for and report on an onerous contract or commitment in line with the requirements of FAS 30 “Impairment, Credit Losses and Onerous Commitments”.

Presentation and disclosure

8. Qualitative disclosures shall be made in respect of ancillary Wa’ad or Khiyar arrangements explaining their nature.

9. Where practical, all significant outstanding ancillary Wa’ad or Khiyar arrangements shall be adequately disclosed under contingent liabilities and commitments (and assets, if applicable) in line with the requirements of FAS 1 “General Presentation and Disclosure in the Financial Statements of Islamic Banks and Financial Institutions”[2].

10. An onerous contract or commitment shall be presented and disclosed in line with the requirements of FAS 30 “Impairment, Credit Losses and Onerous Commitments”.

Accounting for product Wa’ad or Khiyar

Accounting for obligations arising from product Wa’ad or Khiyar

Initial recognition

11. A product Wa’ad or Khiyar shall give rise to a ‘recognised constructive obligation’ in the books of the institution when:

    a. it is ‘more likely than not’ that economic resources will flow out of the institution; and

    b. the institution is able to reliably measure the amount payable at the future date.

12. When the requirements of paragraph 11 are met, duly taking into account factors described in paragraph 24 with regard to the assessment of the probability of the flow of economic resources, the institution shall initially record a recognised constructive obligation at a reasonable estimate of fair value, with the corresponding loss recognised in the statement of income.

[2] Presently FAS 1 “General Presentation and Disclosure in the Financial Statements of Islamic Banks and Financial Institutions”. However, the existing standard is undergoing a revision process whereby an exposure draft of the revised standard has already been issued.

Subsequent measurement

13. The carrying amount of the recognised constructive obligation shall be reviewed at the end of each financial reporting period, and necessary adjustments shall be made. Any gains or losses shall be taken to the statement of income unless these pertain to a Tahawwut arrangement (to be accounted for in line with the requirements of paragraphs 28-34).

Derecognition

14. An institution shall derecognise the recognised constructive obligation when:

    a. it is extinguished i.e. when the obligation has been discharged;

    b. the obligation expires, or is cancelled by the other party; or

    c. it ceases to meet the recognition criteria described in paragraph 11.

15. The institution shall recognise any gains or losses arising on derecognition of the recognised constructive obligation in the statement of income.

Presentation and disclosure

16. In addition to the presentation and disclosure requirements of FAS 1 in respect of recognised constructive obligation and any changes therein, the following are the minimum disclosure requirements in the financial statements of an institution:

    a. the accounting policies adopted for the Wa’ad and Khiyar transactions, as well as related significant judgments and estimates;

    b. the carrying amounts of recognised constructive obligations in respect of Wa’ad and Khiyar arrangements;

    c. the amount of gain or loss recognised in the statement of income; and

    d. the gain or loss on a Tahawwut (hedge) relationship attributed to the hedged item.

Accounting for rights arising from product Wa’ad or Khiyar

Initial recognition

17. A product Wa’ad or Khiyar shall not give rise to a constructive right in the books of the institution unless all of the following conditions are met:

    a. it is ‘highly probable’ that economic resources will flow to the institution;

    b. a legal or constructive obligation exists for the economic resources to flow to the institution; and

    c. the institution is able to reliably measure the amount receivable at the future date.

18. When the requirements of paragraph 17 are met, duly taking into account factors described in paragraph 24 with regard to the assessment of the probability of the flow of economic benefits, the institution shall initially record a ‘recognised constructive right’ based on a reasonable estimate of fair value of the receivable.

Subsequent measurement

19. The carrying amount of the ‘recognised constructive right’ shall be reviewed at the end of each financial reporting period, and necessary adjustments shall be made. Any gains or losses arising on remeasurements shall be taken to the statement of income unless these pertain to a Tahawwut arrangement (to be accounted for in line with the requirements of paragraphs 28-34).

Derecognition

20. An institution shall derecognise the ‘recognised constructive right’ when:

    a. the contractual rights to obtain cash flows from the recognised constructive right expire; or

    b. it ceases to meet the recognition criteria described in paragraph 17.

21. The institution shall recognise any gains or losses arising on derecognition of the ‘recognised constructive right’ in the statement of income.

Presentation and disclosure

22. In addition to the presentation and disclosure requirements of FAS 1 in respect of recognised constructive right and any changes therein, the following are the minimum disclosure requirements in the financial statements of an institution:

    a. the accounting policies adopted for the Wa’ad and Khiyar transactions, as well as related significant judgments and estimates;

    b. the carrying amounts and types of the rights recognised in respect of Wa’ad and Khiyar arrangements and movement therein;

    c. the amount of gain or loss recognised in the statement of income in respect of Wa’ad and Khiyar arrangements segregating the initial recognition effect, and the effect of subsequent reassessments; and

    d. the gain or loss on a Tahawwut (hedge) relationship attributed to the hedged item.

Multiple Wa’ad and Khiyar arrangements

23. Wa’ad and Khiyar arrangements involving Shari’ah compliant bilateral or parallel or multi-lateral or series of Wa’ad and Khiyar arrangements by independent parties shall be accounted for applying the requirements of this standard on each individual Wa’ad or Khiyar separately.

Assessment of the probability of the flow of economic resources

24. To assess that economic resources will flow to or out of the institution, the following factors, inter-alia, shall be taken into consideration:

    a. the legal and regulatory environment under which the institution operates;

    b. the Wa’ad or Khiyar has a significant economic incentive for the counter party;

c. existence of any collateral, security, or guarantee held or placed with / issued by the institution, including any margin and / or variation margin maintained as per regulatory requirements;

d. the practice followed by the industry in similar situations;

e. the fact that the counter party has incurred any cost in good faith based on the promise made by the institution; and

f. the public expectation, and the trust placed on the institution as an upholder of Shari'ah principles and rules and moral values.

Hamish Jiddiyyah and Arboun

25. A product Wa'ad or Khiyar may involve receipt or payment of Hamish Jiddiyyah or Arboun which shall constitute an asset or liability for the respective parties.

26. Hamish Jiddiyyah and Arboun shall be accounted for and reported according to provisions of the relevant AAOIFI FAS.

27. The amount of Hamish Jiddiyyah shall not be netted-off with the recognised constructive obligation or recognised constructive right, unless a legally enforceable right to net off or settle on a net basis is established. Arboun paid may be adjusted with the sales consideration payable / receivable once the sale is consummated / concluded.

Accounting for Tahawwut (hedging) arrangements

28. An institution may designate a hedging relationship between a Wa'ad or Khiyar (referred to as a hedging instrument) and a hedged item where hedging relationship exists, whereby:

    a. the hedged item – is an asset, liability, firm commitment, or highly probable forecast transaction that:

        i. exposes the institution to the risk of changes in the fair value or future cash flows; and

        ii. is designated as being hedged.

    b. the hedging instrument – is a designated Wa'ad or Khiyar, fair value or cash flows of which are expected to offset changes in the fair value or cash flows of the designated hedged item. A Wa'ad or Khiyar may be designated as a hedging instrument if it is made to a party external to the institution.

29. A hedging relationship qualifies for hedge accounting, in line with the requirements of this standard if, and only if, the following criteria are met:

    a. it consists of hedging instruments and hedged items that are formally designated through documentation according to the institutions risk management objectives; and

    b. there is an economic relationship between the hedging instrument and the hedged item.

30. A hedging relationship shall be accounted for in line with paragraph 29 when all of the following conditions are met:

   a. the hedging relationship is adequately documented, identifying the hedging instrument and the hedged item, the nature of the risk being hedged, and how the institution will assess the hedging instruments effectiveness;

   b. the hedge is expected to be effective in achieving its desired objectives that were originally documented in the risk management strategy for that particular hedging relationship by offsetting changes in fair value or cash flows attributable to the hedged risk;

   c. an exposure to variations in cash flows must be probable, in case of cash flow hedges, that may have an impact on the statement of income;

   d. the effectiveness of the hedge can be reliably measured; and

   e. the hedge is assessed on an ongoing basis and is determined to be highly effective throughout the financial reporting period.

31. If a fair value hedge meets the conditions in paragraph 30 it shall be accounted for as follows:

   a. the gain or loss arising from the remeasuring of the hedging instrument at fair value shall be recognised in the statement of income; and

   b. the gain or loss on the attributable hedged item shall adjust the carrying amount of the hedged item and be recognised in the statement of income.

32. If, during the period, a cash flow hedge meets the conditions in paragraph 30, it shall be accounted for as follows:

   a. the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognised in equity (respectively attributable to owners' equity and quasi-equity); and

   b. the ineffective portion of the gain or loss on the hedging instrument shall be recognised in the statement of income.

33. An institution shall discontinue the hedge accounting if:

   a. the hedging instrument expires or is settled, terminated or exercised. The replacement, renewal, or rollover[3] is not an expiration or termination if such replacement, renewal, or rollover is part of the institutions documented hedging strategy. There will not be an expiration or termination of the hedging instrument if:

      i. as a consequence of laws or regulations or the introduction of laws or regulations, the parties to the hedging instrument agree that one or more clearing

[3] If so prescribed under relevant Shari'ah principles and rules.

counterparties replace their original counterparty to become the new counterparty to each of the parties; and

ii. other changes e.g., change in the collateral, rights to offset asset or liability, to the hedging instrument are limited to those that are necessary to effect such a replacement of the counterparty.

b. the hedge no longer meets the criteria for hedge accounting in paragraph 29; or

c. the institution revokes the designation of the hedge.

34. For cash flow hedges other than those covered by paragraph 32, the amounts that had earlier been recognised in equity shall be recycled from the respective equity accounts (owners' equity or quasi-equity) to the statement of income in the same period(s) during which the hedged forecast cash flows affect the statement of income.

Effective date

35. This standard shall be effective for the financial statements beginning on or after 01 January 2022. Earlier application of the standard is permitted.

Appendices

Appendix A: Adoption of the standard

This standard was presented for approval in the AAOIFI Accounting Board's meeting No. 17 held on 5-6 Sha'ban 1441H, corresponding to 29-30 March 2020 and was duly approved.

Members of the board

1. Mr. Hamad Abdulla Al Oqab – chairman
2. Mr. Syed Najmul Hussain – deputy chairman
3. Mr. Abdelhalim Elsayed Elamin
4. Mr. Abdulmalik Abdullah Alsuwayni
5. Dr. Abdulrahman M. Alrazeen
6. Ms. Amal Al Masri
7. Dr. Bello Lawal Danbatta
8. Mr. Firas Hamdan
9. Mr. Hondamir Nusratkhujaev
10. Mr. Imtiaz Ibrahim
11. Mr. Irshad Mahmood
12. Dr. Mohammed Albeltagi
13. Mr. Samet Arslan
14. Mr. Saud Al Busaidi
15. Mr. Yusuf Ahmed Ibrahim Hasan

Reservation

The standard was approved unanimously.

Working group members

1. Mr. Syed Najmul Hussain – chairman
2. Dr. Hussein Said Saifan
3. Mr. Ijlal Alvi

Executive team

1. Mr. Omar Mustafa Ansari (AAOIFI)
2. Mr. Mohammad Majd Bakir (AAOIFI)
3. Mr. Haroon Tabraze (Senior Consultant-Researcher)
4. Ms. Farida Cassim (AAOIFI)

Appendix B: Basis for conclusions

Classification of Wa'ad and Khiyar

BC1 During initial discussion and the preliminary study phase, the working group and the board contemplated on the different ways that Wa'ad and Khiyar transactions may be classified. After due discussion, it was agreed that the best way is to classify based on whether the Wa'ad or Khiyar is ancillary to a product, or a product by itself. The very nature of Islamic finance contracts and arrangements was also considered whereby Shari'ah does not allow combination of two or more contracts or arrangements, if one or more is stipulated as a condition in another contract. Further discussion with the AAOIFI committee of the Shari'ah board for review of accounting and governance standards (the Shari'ah committee) confirmed that combination of contracts is permissible subject to a specific set of conditions. Saying that Shari'ah does not allow such combination across-the-board does not reflect the rulings set out in Shari'ah standards. Combination of two contracts which are neither contingent on each other nor connected with each other is permissible under Shari'ah principles and rules.

BC2 Accordingly, in Islamic finance structures like Murabaha or Ijarah Muntahia Bittamleek, it is normally understood that the core contract is the Murabaha or Ijarah. On the contrary when Wa'ad or Khiyar is used directly as a product, e.g., in case of foreign exchange forward contract based on promise, there is a need to provide for accounting of the product itself.

BC3 The Shari'ah committee also discussed the types of Khiyar that shall be considered to be covered by this standard. It was decided that insofar as AAOIFI standards are principles-based, this standard accounts for various types of Khiyar.

Similar accounting treatment for Wa'ad and Khiyar

BC4 The board discussed and agreed that in most circumstances a Khiyar may give rise to an obligation or create a right in a manner similar to Wa'ad. The main difference, normally, is that a Wa'ad is contained in a separate document while a Khiyar (generally) is embedded in the core contract. Further, Khiyar is used at a stage where the contract has not been concluded yet, while Wa'ad is normally used following an agreement between the two contracting parties. Another difference is that in Wa'ad, compensation to the counterparty may be needed due to the occurrence of damages, etc. while in Khiyar such a compensation mechanism is not available.

BC5 As Wa'ad and Khiyar may give rise to similar economic consequences, the board decided to combine both in the same standard and prescribe similar accounting treatments, as relevant.

Onerous commitments

BC6 The board concluded that normally an ancillary Wa'ad or Khiyar shall neither be recognised as an asset, nor a liability because the main product is recognised, measured, and presented in the financial statements in line with respective AAOIFI FAS and Shari'ah does not allow combination of two or more transactions / future contracts. However, the board further considered the situations where a Wa'ad or Khiyar may result in an onerous commitment and decided that the same shall be accounted for in line with the treatment already provided in FAS 30 "Impairment, Credit Losses and Onerous Commitments".

Accounting for product Wa'ad or Khiyar

BC7 The board considered the fact that Wa'ad or Khiyar that is a product by itself may require recognition and measurement in the financial statements, if there is a probability of inflow or outflow of economic benefits to / from the institution.

BC8 The board discussed the possibilities when a product Wa'ad or Khiyar may give rise to a liability in the financial statements. After deliberation it was concluded that recognition of obligation should be based on more than 50% probability of economic resources flowing out of the institution. Therefore, the board decided to use the term 'more likely than not' as the criteria for recognition of a liability. The recognition of liability on the basis of 'more likely than not' possibility of outflow of economic resources from the institution is consistent with generally accepted prudence principle of recording liabilities / promises.

BC9 The Shari'ah committee and working group evaluated the suitability of the term 'liability' and its alternatives. A 'liability' or an 'obligation' arise from past events, usually on the basis of a contract, when an institution makes a commitment to make a payment. When the obligation is measurable, it is called a liability. The term liability generally connotes that one party is obliged to pay, whereas the other party has the right to receive the payment, arising as a result of a contract. According to Shari'ah, this happens when a Dain is established.

BC10 A 'constructive obligation' arises when one party has intention to make payment, on the basis of past / customary practices or industry norms, without the reciprocal right to receive the payment from the other party. The term 'recognised constructive obligation' was agreed upon because it conveys the nature of the transaction as of a provision, and the institution is recognizing the provision on its own.

BC11 Based on the similar principle as discussed in BC9, it was agreed that 'recognised constructive right' is a better term in relation to 'asset' or a 'constructive asset' as the two latter terms may imply possession or control or establishment of a receivable (Dain) which is not correct in this case.

BC12 The board further decided that the triggering point for recognition of an asset in relation to a product Wa'ad or Khiyar shall be the time when the institution is 'almost certain' of inflow of economic resources. With due deliberations, it was agreed that probability of more than 90% indicates a very high degree of certainty. Therefore, the board agreed to use the term 'highly probable' that represents almost certainty of a transaction to happen. However, it was deliberated that such recognised constructive right might still not meet the definition of an asset from Shari'ah perspective, although it may be an asset in accounting terms

Tahawwut arrangements

BC13 The board deliberated at length as to whether it would be appropriate to include Tahawwut (hedging) arrangements in the scope of this standard. It was observed that institutions are now increasingly entering into Shari'ah compliant Tahawwut arrangements as part of their risk management strategy, which are normally based on Wa'ad or Khiyar arrangements. With respect to their accounting, it was decided that such arrangements should be accounted for similar to product Wa'ad or Khiyar, however, their counter effects should be recognised in line with the treatments similar to generally accepted accounting principles.

Appendix C: Brief history of the preparation of the standard

H1 The newly formed AAOIFI Accounting Board (AAB/ the board) held its meeting No. 1 on 6-7 Jumada II 1437H, corresponding to 15-16 March 2016 at Ramee Grand Hotel, Kingdom of Bahrain.

H2 AAB held its meeting No. 7 on 2 Muharram 1439H, corresponding to 22-24 September 2017 where the preliminary study was presented to the board that addressed the content and structure of the standard.

H3 The working group meetings to discuss the first draft of the standard was held on 11 and 16 Rabi' I, 1440H, corresponding to 19 and 24 November 2018, respectively. In these two meetings the scope and objective of the standard was discussed. The working group then provided its recommendations to the board.

H4 The exposure draft with working group conclusions were discussed at AAB meeting No. 12 held on 29-30 November 2018. The board requested changes and principally approved the exposure draft for issuance.

H5 The third working group meeting to discuss the board requirements and basis of conclusion was held on 3 Rabi' II 1440H, corresponding to 10 December 2018. The exposure draft was finalized and issued on 24 Rabi' II 1440H, corresponding to 31 December 2018.

H6 The public hearing for the exposure draft was conducted in multiple jurisdictions during 2019 and 2020. The first public hearing webinar event for the exposure draft was conducted in July of 2019 in the Kingdom of Bahrain and in the Kingdom of Saudi Arabia (hosted by Saudi Organization for Certified Public Accountants – SOCPA) in October 2019. Additionally, the final public hearings were conducted in the state of Oman (hosted by College of Banking and Financial Studies – CBFS) in February of 2020.

H7 The committee of the Shari'ah board for review of accounting and governance standards held its meeting No. 10 on 15 Rajab 1441H, corresponding to 10 March 2020 where the standard was discussed and after duly taking the views for conformity with Shari'ah presented to the working group for final review.

H8 All comments received from public hearings along with the views and comments from different industry participants on the exposure draft was presented for discussion at the fourth working group meeting held on 16 Rajab 1441H, corresponding to 11 March 2020.

H9 AAB held its meeting No. 17 on 5-6 Sha'ban 1441H, corresponding to 29-30 March 2020 in the Kingdom of Bahrain. All comments and recommendations received on the final version of the exposure draft was presented for discussion at this meeting where the newly appointed board deliberated on changes suggested by the working group and the standard was approved for final issuance.

H10 The standard was approved for publishing with instructions for making suggested changes. After due process, the standard was issued on 30 Rabi' II 1440H, corresponding to 15 December 2020.