

## RESEARCH ARTICLE

# Shariah Appraisal of Margin Trading

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## ABSTRACT

The Islamic finance industry has shown remarkable growth in the last 30 years. However, this growth has mostly been restricted to the banking sector while the Islamic capital market is still at its nascent stage. Several countries have attempted to bridge this gap by introducing various Islamic alternative products to their respective capital markets. However, investors have not been receptive to these alternatives due to the lingering controversies surrounding their permissibility. This study attempts to study margin trading from a Shariah perspective. To achieve that, a step-by-step assessment of margin trading was conducted and the relationship between the brokerage firm and the investor was characterized as *qard*. Two case studies of Islamic margin trading were selected and analyzed from a Shariah viewpoint. The study concludes that the conventional margin trading facility is not Shariah-compliant due to the element of *riba*. There are also some Shariah concerns in the two Islamic margin trading alternatives that were analyzed in the study.

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**Purpose** – There has been a significant increase in the number of retail investors during the current pandemic. The emergence of several commission-free trading platforms has been highlighted as one of the major forces behind it. This increase has also resulted in a rise in the number of people using the margin trading facility. The popularity of margin trading has not extended to Arab and Muslim states even though several companies in Muslim-majority countries such as Saudi Arabia, Qatar, and UAE have introduced Islamic margin trading. The reason for this is that literature addressing the Shariah rulings on margin trading in English is scant. Therefore, this study is a modest attempt to bridge that gap.

**Methodology** – This study is qualitative in nature. Qualitative data were collected and analyzed to reach a ruling on margin trading. This study relies on the literature of four major jurisprudential schools of thought and on the opinions of Islamic institutions and contemporary scholars.

**Findings** – Margin trading offered by conventional financial institutions are not permissible. All the Shariah alternatives of margin trading that were analyzed in this study had Shariah issues and concerns. However, the margin trading alternative offered by The Group Securities in Qatar offers a ray of hope about the viability of using *qard* to structure margin trading.

**Originality/Value** – This paper to the best of my knowledge is the first independent paper in English that attempts to appraise the practice of margin trading from a Shariah perspective.

**Keywords:** margin trading, *qard*, *rahn*, shares, Shariah

## 1. INTRODUCTION

### 1.1 Background

The stock market in Muslim countries remains significantly underdeveloped and highly illiquid despite the abundance of wealth and resources. The adoption of the stock market in its conventional state without any alteration of its modes and structure to conform with Islamic law is one of the reasons for its failure and non-acceptance among the Muslim population.

Muslim-majority countries have taken different initiatives to address this problem. This includes relaxing the rules restricting foreign investors from holding a proportionate part of a company and incentivizing family-owned businesses and companies to list on the stock market. Additional attempts have been made to offer more Islamic-compliant instruments.

Margin trading and short selling have been regarded as controversial instruments in the stock market since time immemorial. An investor who believes that the stock price of a company is undervalued and will likely increase in the future will want to have such stocks to benefit from the future increase in price. In this case, the investor borrows the cash from a brokerage firm. The investor then sells the stocks in the market when the price

of the stocks increase. The purchased stocks are also held with the lender as collateral for the loan.

Recently, few Islamic financial institutions and hedge funds have rolled out what they claim to be Shariah-compliant margin trading. The proponents of these Islamic alternatives view them as ingenious moves that will help facilitate the growth of Islamic hedging and stock markets. Conversely, the detractors of these Islamic alternatives view them as mere replications that attempt to “Islamize” conventional products using existing Islamic contracts. This accusation could be detrimental to the development and acceptance of such Islamic alternatives.

## 1.2 Research Motivation

There is an ever-growing interest in academic circles regarding the role of margin trading. These varying interests stem from the controversies surrounding margin trading. Most papers addressing this topic tend to focus on the role of margin trading in liquidity enhancement and market efficiency. There seems to be a great paucity of English literature assessing the efficacy of margin trading from a Shariah perspective. This study is a modest attempt towards bridging this gap.

## 1.3 Research Methodology

This study is qualitative in nature. Qualitative data were collected and analyzed to reach a ruling on margin trading. The study relies on the literature of four jurisprudential schools of thought and on the work of modern Islamic academics and scholars. A proper Shariah assessment of margin trading can only be performed by looking at the margin trading agreement of each financial institution. The selection for the case study is based on the brokerage firms or other financial institutions that made the margin trading agreements available on their websites.

## 1.4 Literature Review

The paper by Muhammed ElGari,<sup>1</sup> which was presented at the 18th session of the OIC Islamic Academy for deliberation and discussion, is probably the best paper that provides a detailed description on the mechanism of margin trading. The author discusses the various parties involved in margin trading and its rationale and purposes. He asserts that margin trading is a form of gambling in price. He believes that it is not possible for shares to be the item of loan contracts. Short selling is briefly discussed in a few paragraphs in which the author states that when a broker stipulates to retain and benefit from the stocks borrowed, this will be construed as *riba* (interest) and therefore not permissible. He further states that high competition has led Islamic banks to offer margin trading using *Murabaha* (cost-plus financing). In Islamic margin trading, the client identifies certain shares and

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1 Mohammed Ali Elgari, “Tijarat Al-Hamish,” 2006, <https://iefpedia.com/arab/wp-content/uploads/2009/06/d8aad8acd8a7d8b1d8a9-d8a7d984d987d8a7d985d8b4-d985d8add985d8af-d8b9d984d98a-d8a7d984d982d8b1d98a.pdf>.

specifies the amount and quantity. The bank purchases these shares with the hope of selling it to the client at a cost-plus mark-up. The bank also mandates the client to purchase additional stock, which will be held as security. This is like the conventional margin trading in which the broker asks the client to deposit a margin in a margin account. While discussing the Shariah ruling of margin trading, the author states that the combination of debt and sale in one contract is impermissible regardless of whether the loan is with or without interest. The author is also of the view that the normal practice in which the client purchases stocks and pays off his loan on the same day without incurring any interest is permissible from an Islamic point of view.

Alsuhaibani and Abdullah started by describing what margin trading is and how it works in different markets.<sup>2</sup> They highlighted the position of the Fiqh Academy on the impermissibility of margin trading when interest or other charges are involved. The authors examine the benefits that are accrued to the broker in margin trading in return for extending loans. They describe the *fiqh* rulings on margin trading when the transaction is devoid of the element of interest. They conclude by stating that with regards to the benefits in margin trading, the broker is the sole benefactor and the client's benefit is negligible and insignificant compared to that of the broker. Advancing an interest-free margin by the broker to the client will not make it Shariah-compliant as it involves one or more prohibited benefits.

Most of the papers analyzed in this section have provided a detailed description of the mechanism of margin trading but have failed to provide practical applications of Islamic margin trading. This study helps bridge this gap and analyzes some contemporary practices of margin trading.

## 2. MARGIN TRADING

### 2.1 Introduction

The process of borrowing money from a broker or bank to purchase stocks is called margin trading. The US Securities and Exchange Commission defines margin trading as “borrowing money from your broker to buy a stock and using your investment as collateral.”<sup>3</sup> Margin trading allows an investor to invest beyond his capacity by paying only part of the required amount of the deal.<sup>4</sup> The brokerage firm funds the remaining amount. An investor has to open a margin account with his broker to avail this loan.<sup>5</sup> The

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2 Mohammad Alsuhaibani and Al-Omrani Abdullah, “Benefits of Brokers’ Loans: An Islamic Law Perspective,” *Journal of King Abdulaziz University: Islamic Economics* 22, no. 1 (January 1, 2009): 3–40, <https://doi.org/10.2139/ssrn.2275926>.

3 The U.S. Securities and Exchange Commission, “SEC.Gov | Margin: Borrowing Money to Pay for Stocks,” April 17, 2009, <https://www.sec.gov/reportspubs/investor-publications/investorpubsmarginhtm.html>.

4 eBharati V. Pathak, *Indian Financial System* (Pearson Education India, 2014), 219.

5 D. R. D. Davis, *Economic Secrets of the New Retirement EnvironmentTM* (Xlibris US, 2009), 66, <https://books.google.com.kw/books?id=cfyNAAAAQBAJ>.

broker asks the investor to deposit a certain percentage of the value of stocks that the investor seeks to borrow. This amount is called the *initial margin*. The stocks purchased on this margin are held with the broker as collateral and assurance about the ability of the investor to repay the loan. The brokerage firm usually finances margin trading by borrowing money from banks at a low interest rate. This interest is called the *call rate*. The broker in turn lends the amount to the investor by charging him a higher interest rate. The difference between the two interest amounts is the profit of the brokerage firm.

## 2.2 Mechanism of Margin Trading

A broker will ask an investor to deposit an initial margin when he expresses the wish to use the margin trading facility and the two parties will sign a margin trading agreement. This agreement defines the roles and responsibilities of each party. It also determines the interest rate the borrower pays on the margin loan. To finance this, the broker borrows the required amount from a bank and pays a broker call rate. The broker then adds one half of one percent to it which the borrower must pay.<sup>6</sup> This interest is called the *margin rate*, which is compounded on a daily basis.<sup>7</sup>

The agreement also contains a determination of two important margins. The first of these margins is the initial margin which is a percentage of the security the investor wishes to purchase. This margin is deposited in the margin account and could be in the form of securities or money. The level of the initial margin differs across different jurisdictions and is used by regulators as a tool to control the amount of margin loans. The other type of margin is the maintenance margin, which is a minimum amount of equity the investor is required to maintain in the margin account of the market value of shares. The investor's equity is the amount remaining in the margin account after the loan amount and other costs have been subtracted. The broker purchases the identified security on behalf of the investor and holds it as collateral for the loan. If the market value of the security falls below the required maintenance margin, the broker issues a margin call to the investor in which he will be required to deposit additional funds. It is the sole responsibility of the borrower to watch and monitor the margin to ensure full compliance.

## 2.3 Jurisprudential Characterization of Margin Trading (*Takayif Fiqhi*)

Margin trading is a complex contemporary issue that did not exist during the time of the jurists. Normally, a person seeking to determine the ruling of any incident will refer to *fiqhi* literature to see the opinion of scholars on the issue. However, since margin trading has no precedence, arriving at a *fiqhi* ruling will require using a method called jurisprudential characterization.<sup>8</sup>

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6 Michael T. Curley, *Margin Trading from A to Z: A Complete Guide to Borrowing, Investing and Regulation*, vol. 352 (John Wiley & Sons, 2008).

7 Security and Exchange Board of India SEBI, "Discussion Paper on Margin Trading and Securities Lending" (Discussion paper, India, 2002), [https://www.sebi.gov.in/reports/reports/dec-2002/discussion-paper-on-margin-trading-and-securities-lending-pdf-file-\\_13312.html](https://www.sebi.gov.in/reports/reports/dec-2002/discussion-paper-on-margin-trading-and-securities-lending-pdf-file-_13312.html).

8 Shubair defined *takayif fiqhi* as a process "to determine the true nature of new occurrences so as to

### 2.3.1 Characterizing the Relationship between the Broker and the Lender

Margin trading implies borrowing funds to purchase securities. *Fiqhi* literature has special chapters that discuss all matters related to borrowing and lending.

## 2.4 Ruling on Minimum Margin and Initial Margin

Stock market regulation stipulates that investors should have a minimum amount of money in their accounts before entering into a margin agreement. In Qatar, for example, the Qatar Financial Market Authority (QFMA) stipulates that the borrower should provide at least 60% cash fund of the expected value of the trading position.<sup>9</sup> In other jurisdictions, investors are required to deposit the minimum margin before the margin account is opened.

It is important to note that the initial margin in the futures market is different from stock trading.<sup>10</sup> The initial margin in the futures market serves as collateral for the margin loan.<sup>11</sup> However, in stock trading, this margin is part of the transaction value the borrower deposits with the broker.<sup>12</sup>

The initial margin from a Shariah perspective is permissible since it serves as part payment for the shares. The minimum margin that is an additional collateral for the margin loan is also permissible. According to the Malikis<sup>13</sup> and an opinion of the Hanbalis,<sup>14</sup> there is no problem with collateral preceding the act of borrowing. They argue that *rahn* (collateral) is just a security for a loan, and therefore it can come before or after the loan just like a guarantee (*daman*).

### 2.4.1 Pledging of Shares

Stocks purchased on margin are collateralized for the margin loan. This requires a jurisprudential analysis to assess the permissibility, or otherwise, of using shares as collateral for loans.

*Rahn* is the Arabic term for collateral and pledge. It refers to a “property provided in lieu of a debt to a creditor that enables him to take the debt out of the pledged property in cases where the debtor is unable to settle the debt.”<sup>15</sup> The permissibility of *rahn* has been

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categorize them under an original *fiqhi* precept bearing certain characteristics in Islamic jurisprudence, with a view to establishing those characteristics in the new occurrences by virtue of the essential similarities between the original precept and those occurrences” Muḥammad Uthman Shubair, *Al-Takyif al-Fiqhī Li al-Waqā' i' Al-Mustajiddah Wa Taṭbīqātuhu al-Fiqhiyyah* (Damascus: Dār al-Qalam, 2014).

9 Qatar Financial Markets Authority, “Margin Trading Rule” (Qatar Financial Markets Authority, 2019), [https://www.qfma.org.qa/English/RulesRegulations/RulesDox/Margin\\_Trading\\_Rules\\_%202019.pdf](https://www.qfma.org.qa/English/RulesRegulations/RulesDox/Margin_Trading_Rules_%202019.pdf).

10 Muhammad Al-Bashir, *Risk Management in Islamic Finance: An Analysis of Derivatives Instruments in Commodity Markets*, vol. 1 (Brill, 2008), 157.

11 Mubarak bin Sulaiman Al Sulaiman, *Ahkam Attaamul Fil Aswaq Almaliya Almu'asira*, 1st ed. (Riyadh: Kunuz Ishbiliya, 2005), 990.

12 S. Gurusamy, *Capital Markets, (9780070153301)*. (McGraw Hill, 2009), 426.

13 Muhammad al-Dasuqi, *Hashiyat Al-Dasuqi*, vol. 1 (Cairo: Dar Ihya al-Kutub al-Arabi, n.d.), 3:245.

14 Abdullah bin Ahmad Ibn Qudamah, *Al-Mughni* (Riyadh: Dar alam al-kutub, 2015), 4:241.

15 Ibn Qudamah, 6:23..

established in the Quran,<sup>16</sup> Sunnah,<sup>17</sup> and by Muslim consensus.

The relationship between the debtor and the creditor is that of trusteeship. The pledgee (*murtahin*) is only liable for the destruction of the pledged property in case of negligence and transgression. The debtor is responsible for the expenses of the pledged property during the *rahn* period.<sup>18</sup>

The discussion of the *fuqaha* (jurists) on using undivided shares of an asset as collateral is critical to understanding the Shariah ruling on pledging shares. This is because a share represents an undivided share in the ownership of the capital of a corporation. *Fuqaha* have differed on the issue of collateralizing undivided shares of a property.

The underlying property must be saleable and valuable to be considered as a valid object of a *rahn* contract. The general classical principle is that whatever that can act as a subject of sale can be pledged.<sup>19</sup> Accordingly, the stocks of non-compliant Shariah companies cannot be the subject of *rahn*.

For pledging an undivided property, the major Islamic *fiqh* school of thought (*madhahib*), including the Zahiris, are divided into two positions. The Malikis,<sup>20</sup> Shafi'is,<sup>21</sup> Hanbalis,<sup>22</sup> and Zahiris<sup>23</sup> view the permissibility of using an undivided share of a property as the subject of *rahn* regardless of whether the property is divisible or not. The Hanafis, on the other hand, see the impermissibility of pledging an undivided property irrespective of whether the subject is capable of division or not and whether it was pledged to the undivided property partner or to a third party.

After assessing the positions of the two groups on the issue of permissibility of an undivided property as the subject of *rahn*, in my opinion, the position of the first group that sees the permissibility of using an undivided property as the subject of *rahn* is the preferred view (*Arjah*). The evidence provided by them is comparatively stronger than the rest.

Against this background, it can be concluded that using shares as collateral is permissible and does not infringe any Shariah precepts. This is in accordance with the general principle of *fiqh* which states that any property that can be a subject matter of a sale can also be pledged. This also represents the position of the International Islamic Fiqh Academy<sup>24</sup> and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), which clearly states that “it is permissible to mortgage the financial papers and Sukuk which can be issued and transacted according to Shari’ah.”<sup>25</sup>

It is also permissible for the broker to hold the stocks with him as collateral. Scholars

16 Surah Al-Baqarah (2:283).

17 Al-Bukhari (n.d., 2:888 Hadith no. 2378).

18 McMillen (2015).

19 Ibn Qudamah (2015).

20 See Anas (1994).

21 Al-Shafi'i (1973).

22 Ibn Qudamah (2015).

23 Ibn Hazm (1970).

24 International Islamic Fiqh Academy, “Ruling on Stock Market,” *مجمع الفقه الإسلامي الدولي*, May 14, 1992, <http://www.iifa-aifi.org/1845.html>.

25 AAOIFI, “Shariah Standards,” 2017, <http://aaoifi.com/shariaa-standards/?lang=en..>

are unanimous on the permissibility of collateralizing a loan.<sup>26</sup> Their opinion strictly applies to a non-ribawi *qard* since an interest-based loan is not permissible and cannot be collateralized.

### 2.4.2 Benefiting from Pledged Stocks

The stocks purchased on margin are held as collateral. These stocks are used by brokers to generate additional interest. The interest generated is shared between the broker and the client.

Scholars have distinguished between benefiting from the pledged property that has been pledged due to a loan contract and a pledge due to a sales contract. They differ on the issue of whether the permission of the pledger to the pledgee to benefit from the pledged property will make such benefits permissible. The first group of scholars claim that it is impermissible to benefit from the pledged property if the debt is from a loan, but permissible if it is from a sale contract.<sup>27</sup>

The second opinion on this matter is that benefiting from the pledged property is permissible. These scholars do not distinguish between sale or loan contract. This is the view of some Hanafi Jurists.<sup>28</sup> Their argument is that the pledger owns all the benefits of the pledged asset. Therefore, if he chooses to give away this ownership to the pledgee, then it is normal. It will be regarded just as a donation from the pledger to the pledgee.<sup>29</sup> It can be argued that even though the pledger owns all the benefits of the pledged property, giving these benefits to the pledgee will mean that upon settlement of the debt, the pledgee would have received more than he had given out in the loan.<sup>30</sup>

The third opinion on this matter is that it is categorically impermissible to benefit from the pledged property regardless of whether the pledged property has resulted from debt or sale. This is the opinion of some Shafi'is<sup>31</sup> and Zahiris.<sup>32</sup> They argue that the pledgee does not own the corpus of the pledged property as it only serves as a security against a claim. Therefore, it is impermissible for him to benefit from it.<sup>33</sup>

Some contemporary scholars have claimed that such benefits could be permitted if the pledgee pays the market value of the benefits. The pledger would therefore be compensated for these benefits, and the pledgee will not be getting any additional benefits. This eliminates any suspicion of *riba*.<sup>34</sup>

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26 Ibn Abidin and Muhammad Amin al-Dimashqi, "Rad Al-Muhtarala al-Dur al-Mukhtar," *Beirut: Dar Al-Fikr; 1412*), 1995, 10:68; Ibn Juzayy, *Al-Qawanin al-Fiqhiyyah* (Beirut: Dar al-Kutub al-Ilmiyya, n.d.), 342; Abu Ishaq Ibrahim bin Ali bin Yusuf Al-Sharazi, *Al-Muhazzab Fi Fiqh al-Imam al-Syafi'i* (Beirut: Dar al-Kutub al-Ilmiyya, 1995), 3:184..

27 Al-Dardir (1995, 4:245); al-Dasuqi (n.d., 1:3:246).

28 Al-Sarkhasi (1987, 21:106); Zadah (1998, 2:606).

29 Al-Sarkhasi (1987, 21:106); Zadah (1998, 2:606).

30 Musa (2013).

31 Ibn Hajr Al-Haitami (2016, 5:52).

32 Ibn Hazm (1970, 8:89).

33 Itfish and Thamini (1973, 11:220).

34 Abozaid (2018).



The most preferred view, in my opinion, is the first view that sees the impermissibility of benefiting from the pledged property if the pledge is a result of a loan and not a sale contract. Allowing a lender to benefit from the pledged property even by paying the market price of such benefits will likely open the door to evil. Some individuals and institutions can attempt to exploit this and use it as a stratagem to circumvent the prohibition of *riba*. The practice of modern Islamic financial institutions is a great testimony to this. Therefore, it can be considered not permissible for the brokerage firm to benefit from the collateralized stocks held in the margin account as such benefits amount to *riba*.

### 2.4.3 Increase in the Value of Collateralized Stocks

The main purpose of an investor conducting margin trading is to capitalize on the future increase in the market price of stocks. Since securities purchased on margin are collateralized, an increase in the value of these securities will mean that the total value to the *rahn* (collateral) has increased. Another form of increase is when a company announces a stock split, which increases the number of stocks outstanding, but the market capitalization remains the same. Scholars of different *fiqh* schools of thought have discussed the issue of the growth of *rahn* in their *fiqhi* literatures. Their discussion is mainly about whether this growth will be combined with the old pledged property to serve as collateral for the debt.

The *fuqaha* have distinguished between two types of growth in the pledged property. The first type is the connected or endogenous (*muttasil*) growth, which is growth that is inseparable from the corpus of the pledged property such as beauty, knowledge, or weight. All the four major schools of thought agree that the connected growth, which is inseparable, also serves as a pledged property.<sup>35</sup> The other type of growth is the separable growth, which is exogenous to the pledged property such as stock split and appreciation in stock price. Jurists are divided into two groups on whether the sudden increase in the pledged property will be joined to equally serve as a pledge to the initial debt. The majority of *fuqaha* of the Hanafis,<sup>36</sup> Malikis,<sup>37</sup> Shafi'is,<sup>38</sup> and Zahiris<sup>39</sup> state that exogenous addition in the pledged property is not part of the *rahn* and the ruling of *rahn* does not apply to it. Applying this to the context of margin trading will mean that the broker does not have the right to keep any addition in the case of increase in stock price, and such addition must be returned to the borrower. The second jurist opinion forwarded by Hanbalis<sup>40</sup> states that the *rahn* ruling applies to any appreciation in the pledged property, and both the appreciation and principal will be considered as collateral for the debt. This means that an appreciation in the price of the collateralized stocks in margin trading will also be regarded as collateral for the margin loan. The AAOIFI adopts the second opinion and considers all appreciation to automatically serve as collateral with the principal.

35 See Al-Kasani (1967, 152); Al-Sharazi (1995, 105).

36 Al-Kasani (1967).

37 Anas (1994).

38 S. M. al-Khatib Al-Sharbini and al-Khatib (1995).

39 Ibn Hazm (1970).

40 Ibn Qudamah (2015).

In my view, the second opinion is the weightiest. Adopting this will further strengthen the pledgee's claim. In the context of margin trading, the broker is entitled to hold any appreciation in stock prices until when the position has been closed. Furthermore, unlike the market of goods in which prices are stable, the stock market is characterized somewhat by the arbitrariness of stock price movements. The value of the investor's portfolio will change several times during a trading session, which means that adopting the first opinion will be cumbersome and tiring. However, the parties can agree that the pledger can withdraw some part of the security when it reaches a certain level.

#### 2.4.4 Ruling on Margin Trading

Margin trading as currently practiced in various stock markets is impermissible from a Shariah perspective. Brokers charge interests on margin loans and restrict borrowers to trading using their platforms to benefit from the margin loans. This is inimical to the Islamic precepts, which prohibit *riba* and benefiting from loans. Contemporary Muslim scholars and Islamic finance experts are unanimous on the impermissibility of margin trading. The OIC Fiqh Academy in its 18th session held in Makkah on margin trading stated that margin trading is impermissible as it entails several Shariah concerns.

If a person transgresses against Islamic commandments and enters into margin trading agreement, will the contract be regarded as void and therefore will not have any legal standing or implication? Or will it be considered as valid but with only rectification needed? The answers to these questions lie in the argument of scholars on the validity of a loan with invalid stipulation. The first opinion is that the loan is valid while the stipulation is void and should be obliterated. This is the view of the Hanafis<sup>41</sup> and the most popular opinion of the Malikis,<sup>42</sup> as well as an opinion in the Shafi'i<sup>43</sup> and Hanbali<sup>44</sup> schools of thought. This is also the view of several contemporary scholars and academics. They base their opinion on the hadith narrated by Aisha, in which Barira, a slave at the time, came to Aisha to seek her help to emancipate herself. Aisha agreed to help her, but the masters of Barira stipulated that the loyalty (*wala'*) of Barira is kept with them upon emancipation. Aisha asked the Prophet about such a stipulation, which was against the practices of those days. The Prophet asked her to accept the contract but nullified the stipulation. This shows that a contract with an invalid stipulation is valid. The second opinion is that both the contract and the stipulation are void. This is the position of the Malikis<sup>45</sup> and a view in Shafi'i<sup>46</sup> and Hanbali schools of thought. They base their opinion on the claim that the contract is predicated on such stipulations and does not occur without them. Therefore, if

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41 Al-Sarkhasi, *Al-Mabsoot*, 14:35.

42 Al-Dardir, *Al-Sharh al-Saqir*, 3:104; Anas, *Al-Mudawwana al-Kubra*, 4:132.

43 Muhammad Khatib al Al-Sharbini, "Mughni Al-Muhtaj," *Jilid III, Beirut: Dâr al-Fikr*, 1997, 2:31..

44 Ala' addin bin Hasan bin Sulaiman Al-Mardawi, *Al-Insaf Fi Ma'rifat Al-Rajih Minal Al-Khilaf Ala Mazhab Al-Imam Al-Mubajjal* (Kuwait: Gharas Linnashr wattauzi'i, 1956), 11:230.

45 Al-Dardir, *Al-Sharh al-Saqir*, 3:104.

46 Al-Mardawi, *Al-Insaf Fi Ma'rifat Al-Rajih Minal Al-Khilaf Ala Mazhab Al-Imam Al-Mubajjal*, 11:23.

the stipulation is impermissible, then the contract will be impermissible.<sup>47</sup> Based on the above discussion, it can be concluded that margin trading is valid when it occurs, but the parties deserve retribution for engaging in a sinful and illicit activity.

### 3. ATTEMPTS TO CONSTRUCT SHARIAH-COMPLIANT MARGIN TRADING AND SHORT SELLING

There have been several attempts to develop Shariah-compliant margin trading. Most of these attempts have taken place in countries with developed capital markets. The growth of the Islamic finance industry and the increase in the sophistication of Muslim investors are the major driving forces behind this growth. This section contains a jurisprudential assessment of Islamic margin trading practices to ascertain their permissibility.

#### 3.1 Islamic Margin Trading

We have seen that margin trading as practiced in the conventional equity market contains several Islamic concerns. Different financial institutions have attempted to provide an Islamic alternative by overcoming the shortcomings of conventional margin trading. They employ the Islamic concepts of *Murabaha* and *qard* in structuring these alternatives. This study will assess Islamic margin trading offered by two financial institutions: The Group Securities (Qatar) and Mawarid Securities (UAE).

#### 3.2 The Group Securities

The Qatar Financial Market Authority issued rules on margin trading in 2014. Up until October 2016, The Group Securities was the only brokerage firm authorized to conduct margin trading in the Qatar Stock Exchange.<sup>48</sup> The margin trading facility offered by the firm is distinct in that there is only one margin trading agreement that has been structured in a way that will cater to the needs of both conventional and more conservative Muslim investors. To open a margin account with The Group Securities, a client must have an active account with the firm. The account opening occurs at their main office in Qatar.<sup>49</sup>

The two parties have to sign a margin trading agreement that contains the following details:

1. The company provides free financing to clients for a period of 7 working days. The client who can close a position during the 7-day window will not have to pay any interest. The client pays 60% of the initial margin into the margin trading account, with the firm providing the remaining amount.

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47 bi al-Hassan Yahya bin Abi al-Khayr Salim al-'Imrani, *Bayan Fi Madhab Al-Imam al-Shafi'i*, 1st ed., 13 vols. (Jeddah: Dar al-Minhaj, 2000).

48 Satyendra Pathak, "Margin Trading: The Group Draws Massive Response," *Qatar-Tribune* 6 (2016), <http://www.qatar-tribune.com/news-details/id/27244>.

49 The Group, "Margin Trading," accessed March 13, 2020, <https://www.thegroup.com.qa/Margin.aspx?lang=en>.

2. Only stocks listed in the Qatar Stock Exchange are allowed for margin trading. The list contains stocks of both Islamic and conventional financial institutions.
3. The firm gives clients rebate commission and speculation reward trading through the margin trading account.

### **Shariah Concerns in the Structure of The Group Securities**

1. It is impermissible for a client to enter a contract whereby one will have to pay interest after the grace period granted to him even if the client is relatively sure on his ability to repay the loan during the grace period. The Islamic Fiqh Council in its resolution on margin trading stated that “the contract involves an obvious *riba*, which is represented by the addition to the amount of the loan which is called ‘overnight charges.’”<sup>50</sup> The Islamic Fiqh Council’s resolution prohibits margin trading even though the client is not charged any interest if the position is closed before the trading session ends.

Contemporary scholars and institutions have also discussed this condition in the context of a person who borrows money using credit cards with the intention of paying back during the grace period. Banks and other financial institutions provide credits to people through unsecured credit cards, where creditors are not charged if they pay within a certain period. This is, in practice, similar to the margin loan facility provided by the firm. The majority of Muslim scholars see the impermissibility of entering into such loan contracts as it entails provisions and conditions on charging interest. The International Islamic Fiqh Academy in its resolution no. 108 (2/12) on credit cards concluded that “it is impermissible in Shariah to issue an unsecured Credit Card or use it if its conditions include imposition of interest. This is so even if the card bearer has the intention to pay within the grace period that precedes imposition of interest.”<sup>51</sup> The client receives all ownership rights associated with the purchase of stocks. He receives cash dividends, voting rights, and all other rights a stock owner receives.

2. The list contains some companies whose shares can be sold on margin that are not Shariah-compliant. Some companies operate in industries that are deemed non-compliant by all Shariah scholars. It is therefore inadmissible to purchase these stocks on margin using the firm’s platform.

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50 The Islamic Fiqh Council, “The Islamic Fiqh Council 18th Session Examination of the Issue of Margin Trading” (2006).

Overnight charges are interest paid for holding a position overnight. This interest is calculated on a daily basis.

51 International Islamic Fiqh Academy, “International Islamic Fiqh Academy Resolution on Credit Cards,” Pub. L. No. 108 (2/12) (2000).

## Concluding Remarks

The margin trading offered by The Group Securities is impermissible for the following reasons:

1. The stipulation that the investor should pay interest after 7 working days from the trade execution day is inadmissible from a Shariah perspective. Even though the loan is initially an interest-free loan, it might turn to a *ribawi* contract if the investor fails to repay the loan during the assigned time frame. Moreover, as a rule of law, anything conducive to *haram* (forbidden) is itself *haram*.
2. The contract is also inadmissible as it involves a combination of loan and brokerage, which is a commutative contract (*mu'awada*). The *raison d'être* for prohibiting such a combination is that the broker might seek to benefit from the credit given to the client. This is clear from the incentive packages offered by the firm such as the rebate commission and the speculation reward, which are meant to induce people to trade more. This increases the volume of trade and subsequently increases the commission the firm receives.
3. Finally, the fact that the company does not perform any Shariah screening and does not seek to distinguish Shariah-compliant stocks from non-compliant ones makes the practice questionable.

## 3.3 Mawarid Securities

Mawarid Securities is marketed as a fully Shariah-compliant brokerage company domiciled in the United Arab Emirates (UAE). It offers a range of Shariah-compliant investment instruments.

Mawarid's Islamic margin trading employs the Islamic concept of *Murabaha*. The relationship between the broker and the investor in conventional margin trading is that of a creditor and a debtor. From a Shariah perspective, this is adapted as a *qard* contract. However, Mawarid's margin trading is adapted as a sale contract, with Mawarid acting as the seller and the investor as the buyer. The client after approaching Mawarid Securities is asked to sign several forms, some of the contents of which are mentioned below.

### The First Form: *Murabaha* Trading Request and Promise to Purchase Form

The client signs a *Murabaha* margin trading request form, which contains his name, the *Murabaha* value, and duration. The document states that the client will purchase the stocks upon their acquisition by Mawarid. Attached to this document is the purchase document in which the client undertakes purchasing the stocks when they are acquired by Mawarid. The promise-to-purchase form contains a page with Attachment 1 as its heading, which contains the name of the client, the financier, the date, and the details of the stocks. The promise-to-purchase agreement contains several clauses as follows:

1. The client promises to purchase stocks as contained in Attachment 1 the moment the company legally acquires them.
2. The promisor is liable for any shortfall if he refuses to purchase the stocks after the stocks have been acquired by the company. The company will deduct the actual

cost it incurs from the amount deposited by the client and recourse back to the client in case of an insufficient amount.

3. If the client fails to sign the *Murabaha* agreement three days after the company has acquired the shares without any justifiable reason, and the company sells the shares, the company will be indemnified for any shortfall.
4. The company can purchase the stocks under the name of the client and place them in the client's account before the two parties sign the *Murabaha* agreement. The client does not own the shares as Mawarid maintains the full ownership of the shares before the *Murabaha* agreement is signed.
5. The agreement is guided by the UAE law, and anything missing from the promise-to-purchase form will be regulated by the UAE law.
6. The client gives the company absolute authorization to handle his stock account, which enables the company to sell shares available in the margin trading account.

### **The Second Form: The *Murabaha* Agreement**

The *Murabaha* agreement contains a page with Attachment 2 as its heading, which includes the details of the stocks, the seller, and the buyer. The section of stock details consists of the name and number of stocks, the cost of the sold share, the profit, and the total cost of the *Murabaha* contract. The seller's details consist of his name, the authorized signature, the job title, and the date of the signature. The purchaser's details consist of his name, the date, and signature.

The *Murabaha* agreement includes several clauses as follows:

1. The seller sells the shares, and the details of the shares will be available in Attachment 2.
2. The buyer agrees to pay the full purchase price and any other guarantees required.
3. The client agrees to take the full risk and responsibility of the stocks starting from the date of the agreement.
4. If the client fails to make any installment payment or provides falsified guarantees, all the remaining installments become due.
5. The client agrees to pay registration and transfer of ownership expenses and all other expenses associated with the contract.
6. The client pays a 12% late penalty in the event of late payment. The amount received is disbursed to charity under the supervision of the fatwa board.
7. The client approves of having the company deduct the monthly installments directly from his account.
8. The client will sign a new *Murabaha* agreement when the client deposits additional funds after the margin call.
9. The laws of the UAE shall apply to this contract in the event that there is no provision in it to the extent that they do not conflict with the provisions and principles of Islamic Shariah as determined by the Fatwa and Shariah Supervision Authority of the seller.

### The Third Form: The Master *Murabaha* Agreement

The document contains several key pieces of information about the two parties. The company provides its address and name of the contract. The client, on the other hand, provides detailed information about himself, such as name, account number, and other information.

There is a section in the document on the rules and regulations of margin trading. This section has several clauses. The first clause is about the definitions of relevant terms. The second clause is about the nature of margin trading as practiced in conventional institutions, including the definition of margin trading and the role of maintenance and the initial margin.

The third clause is about the nature of Islamic margin trading as offered by Mawarid. The following are some of the key points and comments on these clauses:

- The broker purchases certain stocks that have been identified by the client. The price consists of the stock price plus a mark-up. The stocks purchased and other assets are held as collateral in the margin trading account.
- The maintenance margin must always be within a satisfactory level.

The fourth clause is about the risk of margin trading. It identifies several risks the client faces in the margin trading process.

The fifth clause is about maintenance and initial margins. The initial margin is set at 50%, while the maintenance margin is set at 30%. The company will begin to liquidate the margin trading account if the price of the securities is at the 30% maintenance level.

### Shariah Concerns in the Mawarid Structure

1. The client signs a binding promise. Muslim jurists in general agree that promise (*wa'd*) per se is recommended (*mustahab*) and that fulfilling a promise is a good attribute. However, classical jurists are divided on the binding nature of non-commutative *wa'd*. The Hanafi,<sup>52</sup> Shafi'i, and Hanbali<sup>53</sup> schools of thought and Ibn Hazm<sup>54</sup> of the Zahiri school of thought are of the opinion that *wa'd* is recommended (*mustahab*) but not legally binding or enforceable in the court of law (*qada'a*).<sup>55</sup> Although the promisor is not penalized, he is encouraged to fulfill his promise as breaking of promises is not a noble act.<sup>56</sup> They base their opinion on the hadith narrated by Zaid bin Arqam in which the Prophet (pbuh) said: "If a person promises something to his brother with the intention to fulfill it but then does not do so, and

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52 Al-Kasani, *Badai' Al-Sanai'*, 7:84–85; Badr al-Din Abi Muhammad Muhamud bin Ahmad al-'Ayni, *Umdat Al-Qari Sharh Sahih Al-Bukhari* (Beirut: Sharikah wa Matba'a Mustapha Albabi Alhalabi, 1972), 11:60.

53 Mansur Ibn Yunus Al-Buhuti, *Sharh Muntaha Al-Iradat* (Beirut: Alam al-Kutub, 1996), 3:481.

54 Ibn Hazm, "Al-Muhalla," *Juz IX. Beirut: Dar Al-Alaq* 6 (1933):278.

55 Abu Zakaria Yahya bin Sharaf Al-Nawawiyy, *Rawdat Al-Talibin*, ed. Adil Ahmad and Ali Mi'wad (Beirut: Dar al-Kutub al-ilmiyya, 1992), 5:390.

56 Ibrahim bin Muhammad Ibn Muflih, *Mubdi' Fi Sharh Al-Muqni'*, 1st ed. (Beirut: Dar al-Kutub al-ilmiyya, 1997), 9:15.

does not come at the appointed time, there is no sin upon him.”<sup>57</sup> The second opinion is that *wa'd* is binding and the promisor is legally obligated to fulfill the promise.<sup>58</sup> Ibn Arabi states that fulfilling a promise in all circumstances is the preferred opinion to him, except when one has a valid reason not to do so.<sup>59</sup> These scholars mention several *ahadith* and verses to support their stand. Among them is the hadith narrated by Abu Huraira that the Prophet (pbuh) said: “There are three signs of a hypocrite: When he speaks, he lies; when he makes promises, he breaks it; and when he is entrusted, he betrays that trust.”<sup>60</sup> A third group of scholars take a middle stance between the two polarizing positions. They further diverge into two groups. One group states that a promise is recommended. However, it will be binding if it is linked to a cause (*sabab*) regardless of whether the promisee has undertaken a commitment due to the promise. The other group states that the promise becomes binding if it is linked to a cause and the promisee has undertaken certain commitment due to the promise.<sup>61</sup> This opinion was adopted by the Islamic Fiqh Academy in its fifth session held in Kuwait in 1988, which stated that “a promise is religiously obligatory on the promisor except when there is a valid excuse. It will be legally binding if a promise is made conditional upon the fulfillment of an obligation, and the promisee has incurred some liability. The obligation in this case is determined either by implementing the promise, or by compensating the damage caused due to failure to fulfill the promise without an excuse.”

### Choosing the Weightiest Opinion

After analyzing the opinions of scholars on this matter and the evidence advanced by each group, the preferred opinion seems to be that *wa'd* is not binding unless if it is made conditional upon the fulfillment of an obligation and the promisee has incurred some liability so as not to inflict harm on the promisee. This opinion strictly applies to non-commutative contracts.

Contemporary Muslim scholars have differed on the issue of binding *wa'd* in the *Murabaha* contract. Their opinions can be categorized into three broad groups. The first group states that a binding unilateral or bilateral promise is impermissible.<sup>62</sup> The

57 Sulaiman Abu Dawud, “Sunan Abu Dawud,” *Dar Al-Fikr*, 2000, 5:168 Kitab al-Adab, Bab fi al-'iddah, Hadith no. 4977.

58 al-'Ayni, *Umdat Al-Qari Sharh Sahih Albukhari*, 12:12; Abu Hamid Muhammad ibn Muḥammad Al-Ghazali, *Ihya Ulummuddin*, 1st ed. (Beirut: Dar ibn Al-Hazm, 2005), 3:133; Ibn Al-Arabi Abubakar, *Ahkam Alquran*, 3rd ed. (Beirut: Dar al-Kutub al-ilmiyya, 2003), 4:1788; Al-Mardawi, *Al-Insaf Fi Ma'rifat Al-Rajih Minal Al-Khilaf Ala Mazhab Al-Imam Al-Mubajjal*, 11:152.

59 Abubakar, *Ahkam Alquran*, 4:1800.

60 Al-Bukhari, *Sahih Al-Bukhari*, 2:262 Kitab al-Shahadat, Hadith no. 2682; Muslim bin al-Hajjaj Al-Naisaburi, *Sahih Muslim* (Beirut: Dar al-Kutub al-'Ilmiyah, 2010), 1:78 Kitab Al-Iman, Bab Bayan Khisal Al-Munafiq Hadith No. 2682.

61 Muhammad al-Amin Shanqiti, *Adwa' al-Bayan Fi Idah al-Qur'an Bi-al-Qur'an* (Beirut: Dar ibn Al-Hazm, 2015), 3:438.

62 See Bakr bin Abdullah Abu Zayd, *Murabaha Lil Amir Bishira* (Dar Al-Amal, n.d.), 17; Rafic Yunus



second opinion is that a binding promise is permissible in the *Murabaha* contract.<sup>63</sup> The third opinion is that a unilateral promise is permissible while bilateral promises are impermissible. The latter is the opinion of the OIC Fiqh Academy and the AAOIFI.

In my opinion, the position of the OIC Fiqh Academy and the AAOIFI is the most preferred opinion. Adopting the first opinion will expose Islamic financial institutions to great risk because clients will likely breach their promise if there is a change in market conditions and purchasing the goods after it has been acquired by the financial institution is unfavorable to them. The second opinion, on the other hand, is not acceptable because bilateral promises in *Murabaha* are not permissible.

Therefore, the provision of Mawarid to seek compensation for the damage caused by the breach of promise by the investor is unacceptable and in accordance with the position of the OIC Fiqh Academy and the AAOIFI.<sup>64</sup>

Mawarid *Murabaha* agreements have a penalty clause. Contemporary jurists have differed on the acceptability of including penalty clauses in debt contracts. The majority of jurists believe that penalty clauses in debt contracts constitute *riba* and are therefore impermissible.<sup>65</sup> The Islamic Fiqh Council in its 11th session held in Mecca in 1989 ruled on the inadmissibility of such a condition as it is regarded as *riba*.<sup>66</sup> This is also the position of the Islamic Fiqh Academy. However, the AAOIFI<sup>67</sup> and the Shariah boards of several banks have approved such a condition if the financial penalty proceeds are given to charity.

In my opinion, due to a large number of delinquent clients, adopting the first opinion will likely put many Islamic financial institutions out of business as investors and depositors will avoid them. Some have suggested using the judicial institution to punish willful defaulters, but such a solution is costly and takes a lot of time. Therefore, the penalty clause inserted by Mawarid is permissible according to the second opinion and Mawarid should ensure the proper disbursement of such funds.

As the owner of the stocks, the company always assumes full liability of the stocks upon purchasing them. Therefore, registering the stocks in the name of the client is permissible as it is merely to facilitate the ease of transferring of ownership of the stocks to the client upon

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AL-Masri, "The Binding Unilateral Promise (Wa'd) in Islamic Banking Operations: Is It Permissible for a Unilateral Promise (Wa'd) to Be Binding As an Alternative to a Proscribed Contract," *Journal of King Abdulaziz University : Islamic Economics* 15 (2002): 32; Al Sulaiman, *Ahkam Attaamul Fil Aswaq Almaliya Almu'asira*, 891; Abdullah bin Mohammed bin Abdullah Al-Umrani, "Al-Mustajaddat Fi Ahkam Wa Tatbiqahu Ala Ba'i Al-Murabaha," *Majallat Al-Ulum Al-Shar'iyah*, no. 32 (2014): 107.

63 Yusuf Al-Qaradawi, *Bay' Al-Murabaha Lil Amir Bi Al-Shira Kama Tujrihi Al-Masarif Al-Islamia*, 3rd ed. (Cairo: Maktabat Wahba, 1995), 89; Husam Al-Din Afana, *Yas'alunak 'Anil Mu'amalat Maliya Mu'asira* (Dar Al-Amal, 2018), 61.

64 AAOIFI, "Shariah Standards" Shariah Standard No. 8: Murabaha for a Purchase-Orderer.

65 Afana, *Yas'alunak 'Anil Mu'amalat Maliya Mu'asira*, 3:230.

66 Abdullah Ibn Munay, "Matl Alghani Zulm," *Majallat Albuhs Alfiqhiyah Al-Mu'asira*, no. 12 (February 1992): 29.

67 AAOIFI, "Shariah Standards," 89 Number: 2/1/8.

signing the *Murabaha* agreement. However, transferring the stock directly to the account of the client before the *Murabaha* agreement has been signed is not permissible. The fatwa of the Shariah board of AlBilad Bank has stated that “transfer of stocks to the investor’s portfolio prior to ratification of the *Murabaha* agreement is not permissible.”<sup>68</sup>

The International Islamic Fiqh Academy in its sixth session held in Jeddah in 1990 issued a fatwa approving the stipulation that the outstanding installment will become due if the client fails to make any payments. Other contemporary Islamic scholars also give a similar fatwa.<sup>69</sup> However, the Permanent Committee for Scholarly Research and Ifta rule that such a condition is impermissible as it defies the essence of the contract.<sup>70</sup>

The shares in the margin trading account are held as a pledge for the deferred purchase price. In contrast to hypothecation where the borrower uses the securitized property, the client in this margin trading agreement cannot use the shares before the settlement date (*rahn alhiyazi*). Muslim jurists have differed on the permissibility of pledging the sold property if the price of the property is deferred. The opinion of the majority of the scholars of the Hanafi, Maliki, and Shafi’i schools of thought and the most popular opinion of the Hanbali school of thought are that the seller cannot hold the sold property as a pledge for deferred payment.<sup>71</sup> A second opinion of the Hanbalis is that the sold property can be pledged against the payment of the deferred price.<sup>72</sup> This opinion was adopted by the Islamic Fiqh Academy in its 14th session held in Qatar in 2003, which stated that “the seller may require the buyer to pledge the sold property with him to ensure his right to collect the deferred installment.”<sup>73</sup> This is also the position of the AAOIFI.<sup>74</sup> Accordingly, the provision set by Mawarid to keep the pledge property is permissible.

## Concluding Remarks

The *Murabaha* Islamic margin trading satisfies all but one of the requirements of a valid *Murabaha* as set by several Islamic bodies. The main issue with the *Murabaha* structure

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68 Bank AlBilad, *Al-Dawabit Al-Mustakhlasa Min Qararaat Al-Hai’a Al-Shar’iya Libank AlBilad*, 1st ed. (Riyadh: Dar Al-Maiman, 2013), 29.

69 Muhammad Taqi Usmani, *Buhus Fi Qadaya Fiqhiya Mu’asira*, 2nd ed. (Damascus: Dar al-Qalam, 2003), 34; Husam Al-Din Afana, *Bay’ Al-Murabaha Lil Amir Bi Shira- Dirasa Tatbiqiyya Fi Dau Tajruba Sharkat Bait Al-Mal Al-Falastini Al-Arabi* (Palastine: Sharkat bayt Al-Maal Al-falastini, 1996), 121; Dibyan bin Mohammed Al-Dibyan, *Almu’amalat Almaliya Asalat Wa Mu’asara* (Riyadh: Maktaba Almalik Fahad Alwataniya, 2010), 537.

70 Permanent Committee for Scholarly Research, *Fatawa Al-Lajna Al-Da’ima Lilbuhus Ilmiya Wal Ifta*, ed. Ahmad bin Abdullah Al-Darwish (Riyadh: Dar Al-Ma’yid lil Nashr wattauzi’, 2003), 15:275.

71 Al-Sarkhasi, *Al-Mabsoot*, 12:192; Al-Kasani, *Badai’ Al-Sanai’*, 5:249; Muhammad bin Abdullah al-Kharashi., *Sharh mukhtasar Khalil lil Al-Kharashi* (Beirut: Dar Al-Fikr, n.d.), 5:159; Al-Mardawi, *Al-Insaf Fi Ma’rifat Al-Rajih Minal Al-Khilaf Ala Mazhab Al-Imam Al-Mubajjal*, 4:460; Al-Nawawiyy, *Rawdat Al-Talibin*, 3:183.

72 Al-Mardawi, *Al-Insaf Fi Ma’rifat Al-Rajih Minal Al-Khilaf Ala Mazhab Al-Imam Al-Mubajjal*, 4:460.

73 International Islamic Fiqh Academy, “Qarar bisha’an Mushkilat al-Muddakharat fil Al-Mu’assat Al-Maliya Al-Islamiyya,” Pub. L. No. 133 (7/14) (2003), <http://www.iifa-aifi.org/2131.html>.

74 AAOIFI, “Shariah Standards,” 213 Shariah Standard No. 8: *Murabaha*.

lies in the fact that the stocks are not properly possessed by the company before the ratification of the *Murabaha* agreement. It will be therefore appropriate that the company holds the securities in the portfolio before transferring it to the client after the *Murabaha* agreement has been signed.

#### 4. CONCLUSION

The recent coronavirus pandemic has resulted in a huge stock market drop. This has brought back the debate on the role of margin trading and short selling in a financial crisis. The results obtained in different academic studies on margin trading and short selling are mixed. Some claim that margin trading and short selling facilities lead to volatility and instability in the stock market. Many researchers, on the other hand, argue that margin trading and short selling are critical for an efficient market because they help bring market prices closer to their fundamental levels and increases liquidity.

Many pensioners and individuals have lost millions of dollars due to the crisis. Short sellers, on the other hand, have been cashing big from the crisis, with reports showing some hedge funds making billions of dollars from betting on the fall in stock prices; however, there is no contribution towards the development of the stock market or the economy in general.

This study attempts to assess conventional margin trading and short selling from a Shariah perspective. To achieve this objective, the study characterizes the relationship between the client and the broker in margin trading as *qard*. This leads to the conclusion that the margin trading facility offered by conventional financial institutions is impermissible. The study also arrives at several conclusions with respect to margin trading as follows:

1. It is impermissible to charge interest in return for offering margin financing.
2. The stipulation that the stock purchased on margin must be traded through the lender is impermissible. Shariah prohibits the combination of a loan with a sale contract.
3. Undivided share in a property can be the subject matter of *rahn*. Therefore, it is permissible to collateralize the shares of corporations.
4. The broker cannot benefit from the securities held as collateral. Dividends and any additional benefits of the collateralized stocks belong solely to the client.
5. The client cannot receive any interest from the collateralized stocks in the form of rebate as this constitutes *riba*.
6. A pledgee can sell the pledged property with the permission of the pledgor. Therefore, it is permissible for the broker to sell the pledged stocks if the client fails to pose additional funds after the margin call has been issued.

Two Shariah alternatives of margin trading were also assessed. Unfortunately, however, all the Shariah have several Shariah issues and concerns. The Islamic concepts of *qard* and *Murabaha* were used for developing these alternatives. However, these novel practices showed that structuring a fully Shariah-compliant margin trading is feasible. In this regard, after addressing several Shariah concerns in the conventional margin trading,

Mubarak Al Sulaiman stated that it is possible to structure and develop a Shariah-compliant margin trading using the concept of *qard* if the financing is interest-free and from a third party other than the broker.<sup>75</sup> We have already seen the structure of The Group Securities that offers an interest-free loan with a 7-day grace period. The 7-day interest-free margin loans provided by the firm offer a ray of hope and show the economic viability of using *qard* to structure margin trading. The government can partner with brokerage firms during the time of an economic downturn and contraction to offer an interest-free margin loan to high-net investors. Such packages will help revitalize the economy and restore investor confidence.

Using *Murabaha* to purchase order is an ideal way to provide an Islamic-compliant margin trading. It overcomes several bottlenecks of using *qard* structure and provides necessary incentives to both financial institutions and clients. The major Shariah concern in Mawarid's margin trading can easily be resolved. Mawarid should also take a proper possession of the stocks by transferring them to its portfolio before selling them to the client. Therefore, a viable *Murabaha* alternative already exists in the market and other financial institutions wishing to provide *Murabaha* margin trading can replicate it.

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75 Al Sulaiman, *Ahkam Attaamul Fil Aswaq Almaliya Almu'asira*, 997.

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