



**National Zakat
Foundation™**

Zakat on share investments

Determining a proxy for calculation

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This report outlines the juristic precedence determining a proxy for calculation of Zakat on share investments, the methodology, the findings and the recommendations for Muslim shareholders for calculating their Zakat liability.

Summary recommendations

National Zakat Foundation's (NZF) recommendation to Muslim shareholders is as follows:

Ideally, a complete calculation and review of the balance sheet should take place to determine precise Zakat liability on any Sharia compliant shareholding. However, due to the technicalities and difficulties in this, a person may use a proxy of **25%**.

When using the proxy, calculate 2.5% of 25% (0.625%) of one's entire shareholding and pay the sum as Zakat.

This proxy cannot be used by shareholders of private limited companies. Likewise, a small company or start-up which is known to have only cash assets, should not use this proxy. Limited companies, start-ups and general partnership companies may contact NZF to work out their Zakat liability.

*Note: The previous NZF recommendation of **40%** is no longer applicable. Each year the proxy is revised to keep up to date with the most accurate representation of the composition of listed companies.*

Introduction

It has become common for Muslims to own shares as investments. As a result, questions relating to the Zakat treatment of share investments are raised annually. It is common knowledge that listed companies are composed of several assets, some of which are clearly Zakatable, and on the other hand, companies have a list of creditors and debts, some of which are clearly deductible in a Zakat calculation. However, it becomes extremely complicated for the average Muslim shareholder to discern what is Zakatable and what is deductible in a company. Understanding and interpreting financial data is a specialised skill set. Furthermore, for a Zakat calculation service to advise payment on 100% of the shareholding value, is inaccurate and unfair, as we know with certainty that 100% of the assets are not Zakatable. Thus, the middle path seems to be using a percentage as an estimate and proxy, which confidently covers one's Zakat liability on the preponderance of probability.

Juristic precedence for a proxy

If calculating one's Zakat liability on shares is difficult, the use of an estimate has been endorsed by the AAOIFI Sharia Standard No.35 on Zakat. The article 4/2/4 states:

“If it is possible to know through the company what is the exact amount of Zakatable assets (cash, articles of trade and repayable debts) per share, Zakat can be levied on that amount, otherwise Zakat is to be levied on the portion of Zakatable assets per share, **which has to be reached through estimation.**” (AAOIFI 2015)



The proxy is an estimation. In Islamic law, finding a proxy and estimation to make matters easier for people is supported by the following legal case regarding the impacts of impure substances on small and large bodies of water. What is interesting about this legal case is that it is regarding ritual purity and impurity – the foundation of all worship. A legal principle among many jurists is that legal amounts and rates are based on revelation, and if revelation is silent, the judgement is left to the onlooker to apply their discretion. However, the Hanafi jurists suggested a specific amount to determine a large body of water based on experience to make it easy for people. The detail of the legal case is as follows:

The position famously narrated from Imam Abu Hanifa is that a large body of water is what the onlooker considers a large body of water. The onlooker uses his own judgment to determine whether filth affecting one side would affect the other. If he believes it will not, it is considered a large body of water [Tumurtashi, Tanwir al-Absar]. It is also said that Imam Muhammad went back on his original position and adopted the position of Imam Abu Hanifa. [Haskafi, Durr al-Mukhtar].

This is based on a key principle of Imam Abu Hanifa that legal estimations are to be based on revelation and if revelation has not stipulated anything, then estimations are consigned to the judgment of the onlooker. [Ibn Humam, Fath al-Qadir; Ibn `Abidin, Hashiya]

The Fatwa position

Despite the above, most later authorities of the school stipulated that a large body of water is one that is more than 25 square meters in surface area. This position was chosen by the likes of Imam Mawsili in his Ikhtiyar, Sadr al-Shari`ah in his Sharh al-Wiqayah, Imam Marghinani in the Hidayah, and Qadhi Khan in his Fatawa. This is also the original position ascribed to Imam Muhammad. [Ibn `Abidin, Hashiya]

The reason behind stipulating this was to make things easier on the laity and not burden them with the task of making such judgments. The scholars understood that leaving the matter to the laity could cause them hardship, misgivings and doubts. [Ibn `Abidin, Hashiya]

Finally, it should be noted that this estimation was not randomly selected but follows from the original position of Imam Abu Hanifa. **The scholars based their estimation on experience** to determine what surface area is generally required to prevent filth from spreading to the other side of a body of water when originally affecting only one side. [Mawsili, Ikhtiyar]

The methodology of analysing balance sheets

To establish the proxy for shares, the in-house NZF scholars meticulously researched the FTSE 100 companies in consultation with accountants and financial analysts. Each company's assets and liabilities were reviewed from a Zakat perspective.

When analysing the balance sheets of listed companies, NZF looked into the Zakatable nature of each item. Assets which were clearly Zakatable were included in all calculations. Assets which were clearly non-Zakatable were omitted. However, some assets were unclear and therefore termed as 'speculative' assets – assets which are possibly Zakatable but cannot be determined with conviction and certainty.



In terms of the liabilities, only the current liabilities were considered in Zakat calculations. Non-current liabilities were omitted as they are not payable in the current financial year. Similarly, most companies had two types of liabilities: operational and financial. Operational liabilities refer to trading liabilities such as tax, trade payables etc. Financial liabilities refer to debt financing and interest borrowings. Many companies were disproportionately leveraged, and many had interest borrowings – this feature is unfortunately the norm of many companies who operate in trade cycles with debt financing products. The juristic reasons for which debts are deductible are not found in such financial debts [NZF will be releasing a research paper on liabilities and debts in the near future].

To reflect the above variables, we conducted eight different calculations on listed companies in the FTSE 100.

Note: Speculative refers to assets we feel are Zakatable but are not certain. Conservative refers to assets which are Zakatable with certainty.

1. Speculative approach

In this approach, we considered all possible Zakatable assets and all possible deductible liabilities regardless if they were debt financing products.

2. Conservative approach

In this calculation approach, only those assets were included which were clearly Zakatable. Likewise, only those current debts were deducted which were clearly deductible regardless if they were financial or operational in nature. Zakatable assets included cash, receivables and inventories. Deductible liabilities consisted of loans, borrowings, trade payables and tax.

3. Speculative assets without any deductions

In this calculation, we considered all possible Zakatable assets. No deductions were made. This was in line with some schools of jurisprudence which do not advise on deductions.

4. Conservative assets without any deductions

In this calculation, we considered those assets which were clearly Zakatable. No deductions were made. This was in line with some schools of jurisprudence which do not advise on deductions.

5. Speculative assets minus financial liabilities only

In this calculation, all possible Zakatable assets were included. In terms of liabilities, only current financial liabilities were deducted. This was done to get an understanding and comparison of the impact of this variable on a Zakat calculation.

6. Conservative assets minus financial liabilities only

In this calculation, only clear Zakatable assets were included. In terms of liabilities, only current financial liabilities were deducted. This was done to get an understanding and comparison of the impact of this variable on a Zakat calculation.



7. Speculative assets minus non-financial liabilities

In this calculation, all possible Zakatable assets were included in the Zakat calculation. All current liabilities were deducted except debt financing products.

8. Conservative assets minus non-financial liabilities

In this calculation, we considered those assets which are Zakatable with certainty. All current liabilities were deducted except debt financing products.

Upon analysing the variables, data and juristic principles, we proceeded with the data from the calculations based on the formula of: speculative assets minus non-financial liabilities.

This was selected as a precautionary measure for assets to ensure everything that can be Zakatable is considered. In terms of liabilities, debt financing products were omitted from deduction due to the presence of interest payments as well as the fact that such debts do not fall under the juristic rationale for debt deduction.

Findings

Upon analysing the data, we found that **66 of the companies** from the FTSE 100 had a **Zakatable net asset percentage below 25%** - that is two-thirds of the companies have a ratio of less than 25% of company net assets as Zakatable assets. The remaining 33 companies were mainly composed of non-Sharia compliant financial companies such as banks, insurance companies and gambling companies who had a larger proportion of cash assets. From a Fiqh perspective, adopting 25% as the proxy is supported by the jurisprudential maxims:

“The entirety [of something] is given the ruling of the majority”

“The preponderant assumption is in the ruling of certainty”

In conclusion, due to the technicalities and difficulties in calculating Zakat on their shares, a person may use a proxy of 25%. When using the proxy, calculate 2.5% of 25% (0.625%) of one's entire shareholding and pay the sum as Zakat.

For all enquiries, please contact zakatquery@nzf.org.uk