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Budget 2024: halal mortgages

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In the 2024 federal budget released on April 16, the federal government stated its intention to explore new measures to expand access to alternative financing products, like halal mortgages to promote homeownership for Canadians. Consultations with financial services providers and diverse communities have begun so that the government can better understand what federal policies may be put in place to better support the unique needs of all Canadians seeking to become homeowners.

What you need to know

- Permitting new financing arrangements, like non-interest based home mortgage products that are also compatible with the Muslim faith (halal mortgages), would allow many Muslim Canadians to also purchase and finance a home.
- These products could also be made available and utilized by non-Muslim Canadians who would find the terms attractive like any other financial products.
- New measures could include a regulatory sandbox for financial services providers, as these finance arrangements raise tax and consumer protection issues for all lenders, mortgage guideline and other risk issues for federally regulated financial institutions.
- Halal mortgages, while consistent with Islamic financing principles, would ultimately be subject to Canadian law like any other financial product or service.

Background and types of halal mortgages

Islamic finance is based on financing principles that prohibit interest (riba), speculation (maisir), and uncertainty (gharar). It emphasizes risk-sharing, mutual cooperation, and avoiding unjust enrichment or unfair exploitation. Money is seen as a means of exchange, not a commodity itself from which to generate profit, and transactions must be founded upon tangible assets or services. A halal mortgage would allow Muslim Canadians to purchase and finance a home while complying with their faith.

Islamic financing is growing and facilities have been offered for many years in countries with large Muslim populations. In 2019, Islamic finance assets were estimated to total US $2.8 trillion, spread across over 80 countries[1]. Over the last ten years, Islamic finance has grown at a yearly pace of 10%–12%. According to Arab News' 2019 State of Global Islamic Economy report, the total Islamic finance assets are estimated to grow to $3.5 trillion this year[2]. The majority of these assets are concentrated in the Middle East and North Africa, which are home to 190 Islamic banks[3]. The United Kingdom is the biggest centre for Shariah-compliant financing in the western world, and also has the world's first actively managed equity Shariah-compliant exchange-traded fund (ETF) that was launched in September 2020[4]. There are five licensed Islamic banks in the United Kingdom, and over 20 conventional banks that offer Islamic finance products. Other European countries including Luxembourg, Germany, Switzerland and France are also entering the market[5].

In halal mortgages, homeowners still make payments toward the purchase of their home like with a conventional mortgage—but the structure of the mortgage is different. There are three structures that are most commonly used:

1. **Declining balance partnership (Musharaka):** In this structure, registered ownership of the home is with the borrower, but the beneficial ownership of the home is a partnership or co-ownership between the lender and the borrower. Each partner or co-owner contributes capital and shares profits and losses according to their equity interest. The payments are a combination of 1) rent for the portion of the home owned by the bank, and 2) a home equity purchase payment. Over time, the proportion of the property owned by the borrower increases, until the borrower owns the entire interest in the home at the end of the term.

2. **Rent-to-own (Ijara):** A rent-to-own arrangement where the bank acquires the home and leases it back to the borrower. The borrower gradually acquires ownership of the home through periodic lease payments, which are a combination of rent, repayment of principal, and profit for the bank. At the end of the term, the entire ownership in the home is transferred to the borrower.

3. **Sale at a mark-up (Murabaha):** A cost-plus financing arrangement where the bank purchases the home and immediately sells it to the borrower at a markup, with payments made in installments.

Opportunities

While there are some financial institutions in Canada offering mortgages and other financial products that are compliant with Islamic law, they are not currently offered by Canada's "big five" banks. The opportunities available are sizeable—there are more than two billion Muslims around the world, and according to the 2021 Canadian census, Muslims make up almost 5% of the total Canadian population.

Current challenges in implementing halal mortgages in Canada

The market for Islamic finance is less developed in Canada than it is in other parts of the world, and finding halal financing for Muslims in Canada has been difficult. Because few institutions offer halal mortgages in Canada, costs for customers have been higher or many of these Canadian families have been shut out of home ownership altogether.

Institutions in Canada must also navigate a complex matrix of federal and provincial legislation to determine compliance with applicable laws while ensuring that they are consistent with Islamic financing principles. In the absence of targeted legislation, it is challenging to ensure such financing options comply with tax, consumer protection and mortgage laws. Additionally, federally regulated financial institutions face uncertainty around mortgage guideline and other risk requirements.

What's next

Government consultations with financial services providers and diverse communities began in March 2024. New measures could include changes in the tax treatment of these products or a new regulatory sandbox for financial service providers, while ensuring adequate consumer protections are in place. The government has indicated that it will provide a further update in the 2024 Fall Economic Statement.

FOOTNOTES

To discuss these issues, please contact the author(s).

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