



## **Comparative study put option on the Iranian regime and Common law**

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### **ABSTRACT**

The objective of this research was a comparative study of Option (Finance) in the Iranian system and common law. In Iran, the issue of diversification of financial instruments, including option contracts, in addition to the problem of the capital market structure is also faced with the problem of compliance with Islamic rules, because according to the fourth article of the Constitution, all civil, criminal, financial, economic, administrative, cultural, military, political, etc., laws must be based on Islamic criteria. Option securities can play a major role in the efficiency of capital markets. One of the results of this research is that the Iranian capital market because of the lack of diversity in supplied financial instruments has not been able to attract investment in the economy as it should be, and with only a type of financial instrument (common stock) has not been successful in meeting the investors' different needs and trends. On the other hand, it can be inferred that the option contract in Iran capital market as one of the most important and latest derivatives, can play a very important role in the stock market efficiency, risk management, costs reduction and ultimately attracting investors with different interests.

**Keywords:** Option, Securities, Option buying and selling, Investee

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### **INTRODUCTION**

Achieving the objectives that are expected from the market depends on the process that its prominent characteristic is economic growth through innovation and invention. In this process, the behavior of economic activists and consumers is not fully predictable and providing newer and cheaper products from competitors and attracting enterprise customers from competitors are considered a serious threat. Economic theorists and researchers believe that the economic activity is affected by two sections of the financial activities and production activities. Based on the theoretical principals and the results of studies regarding the relationship between the financial sector and the manufacturing sector in economy, not only the effect of positive financial development is confirmed in economic growth and development, but in the causal relationship between these two parts, the financial markets development has a priority [1-4]. In the Islamic world, Option contracts in a new legal entity position have caught the attention of the religious authorities and different views have been expressed about its legitimacy [5-9]. Using Option contract in Iran capital market as one of the most important and latest derivatives can play a very important role in the stock market efficiency, risk management, costs reduction and ultimately attracting investors with different interests.

### **RESEARCH HYPOTHESES**

1. Apparently option contract has an important influence on risk control in product markets.
2. It seems that, Iran and the common law principles of Option contract, do not match well.
3. Apparently, Iran by maximum use of the option contract must coordinate its law rules with the rules of common law.

### **Opinion (Finance)**

Opinion is a contract under which the buyer, by providing the payment to the seller, without being committed to such a purchase or sale in the future, earns the right to buy or sell a specific asset at a certain price.

### **Option transaction by using the final information and comparative study in America and Iran rights**

Option contract by using the final information, like stock exchanges contract, is the most common violations that occur in the securities markets and can deprive the public confidence in capital markets and will stagnate the derivatives markets; therefore, most of the legal systems have prohibited the option contract by using the final information. United States of America in dealing with these transactions is of leading countries. The courts in America have inferred the ban on trading securities by using the final information from sections (b10) and (e14), Securities Market Act 1934 and of the b10-5 and e14-3 Exchange and Market Commission rules.

But in Iran, with approving Islamic Republic of Iran Securities Market Act, transactions of securities by using the final information were prohibited and punishable.

Iranian rights in this regard can, by the sum of the experiences of European and American countries, find the effectiveness minimums in this field.

#### ***A jurisprudential analysis of principle of good faith in the option contract***

In the jurisprudential system, the equivalent of the good faith principle is "Beneficence rule (Qaede-ye-Ehsan)" that is based on the goodness and benevolence and can be inferred from this principle that each legal and worshipping act should be based on charity.

Generally good faith is behavioral; and expresses belief that, in compliance with legal rules, will allow the beneficiary get rid of law violence and drought.

In Iran option contract rights, no signs of goodwill have been observed, but in American rights, goodwill and fair action are the requirements of the rights of this country.

#### **The Concept of Option Contract and Its Variants**

Option buyer according to the type of contract that is signed with the seller, acquire the right to buy or right to sell a certain property. For example, if an individual in order to purchase 1000 sets of Teflon cookware of a factory in Iran, 120 thousand tomans per each set, for 3 months, pays one million tomans and reserves this right up to three months.

In the example above, one million tomans price is considered as the price of opinion and the Teflon dishes that will be in the transaction process in future as the objects of sale are called the underlying asset. And the amount of 1,000 sets of Teflon dishes is called the volume of contract. And the total amount of the contract is 120 million tomans is called agreed price or exercise price; deadline to apply the so-called option contract is called expiration date or maturity option.

#### **The benefits of using option in Iranian and American market**

The benefits of using option can be summarized as follows:

- a- Options market has the ability to give a chance to people, who are willing to risk less, to transfer the risk to those who are seeking higher risk. Given that this market has many influences on reallocation of risk between investors; no one is forced to endure a level of unpleasant risk.
- b- Although the option market does not provide a definitive estimate of the future price of desired items, it can offer information about the volatility of commodity price. In fact, option trading price represents the market expectation of the future volatility of commodity prices.
- c- Option market has lower transaction costs compared to the stock market. This means that for the traders of this market, the commission fee and other transactions costs are less.
- d- Options market allows investors to short sell easily. Considering that investors in stock market have restrictions in line with short selling, many investors instead of short selling in the stock market began to trade option securities.
- e- Using option will increase the efficiency of stock exchange market, because the prices of the goods that option is performed on them reflect their real economic value more accurately

### **RESULTS AND DISCUSSION**

1. According to the Imamieh jurisprudents, the generality of trading discipline is considered an essential expedient and intervening in it, is not allowed. Because its disruption will cause confusion in people's livelihoods. In this case, adherence to a tool like option may be approved by the system very well, because this will stabilize the market and reduce the production risk.
2. Achieving an efficient use of resources in a developed economy, can only be done when individuals and enterprises in pursuit of their own goals, act according to price signals. Economic coordination in the market could be stimulated through the price mechanism. Because prices are constantly and incessantly transferring information about the others willingness and supply and demand to the activists in the market.

3. The main characteristics of competitive institutions regarding the tools such as option, are as follows:
  - a. Decentralized decision-making structure guarantees the freedom of decision-making and economic activists' individual freedom.
  - b. Decentralized structure of competitive decision-making might coordinates economic people's actions and reactions and is the factor of getting scattered information of the market and their optimal use.
  - c. Decentralized structure of the competitive decision-making will increase the efficiency of market forces.
4. The option contract is a required contract and the contracting parties cannot dissolve it arbitrarily, except in cases the right to terminate is specified by law for him, or the right to terminate the contract be predicted. Despite the problems that jurists and common authors have mentioned about the option contract, this contract similar to the American contracts is not dependent on chance, possibility and luck and problems such as being uncertain and gambling are not relevant to this contract; since the contracts titles are not exclusive, based on common jurisprudence this contract may be considered as valid contracts.
5. In terms of option descriptions, option contract generally in accordance with English law, without dependence on a specific market should be considered as necessary, definite, reciprocal (swap), covenant, immediate and decisive contract.
6. Since the feasibility of using option has already been studied from the religious dimension, the researchers, assuming its legal dimension executable, have designed a conceptual model for option using feasibility and have paid attention to conceptual aspects of the technical and structural aspects and market assessing in the Tehran Stock Exchange market. Which is very similar to the US financial markets.
7. Advantage of future standardized contracts gives this feature to them that be neutralized with a reverse contract. Futures prices of foreign currency can be expressed as volume or amount of dollar. Therefore futures trading contracts, both in Iran and America rights, have the advantage of being standardized.
8. Foreign exchange can be regarded as the exchange of two types of purchase power that currencies in the transaction are the documents of that contract. It can be concluded that all the things that we express about the legal review of futures contracts and goods options, can be mentioned in line with the type of foreign currency in these contracts.

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