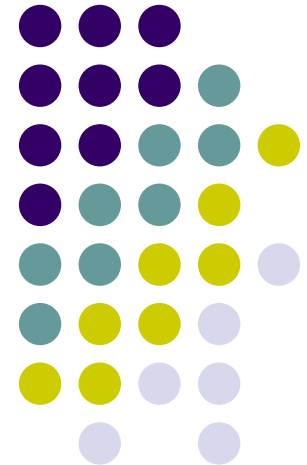


APPLIED SHARI`AH IN FINANCIAL TRANSACTIONS

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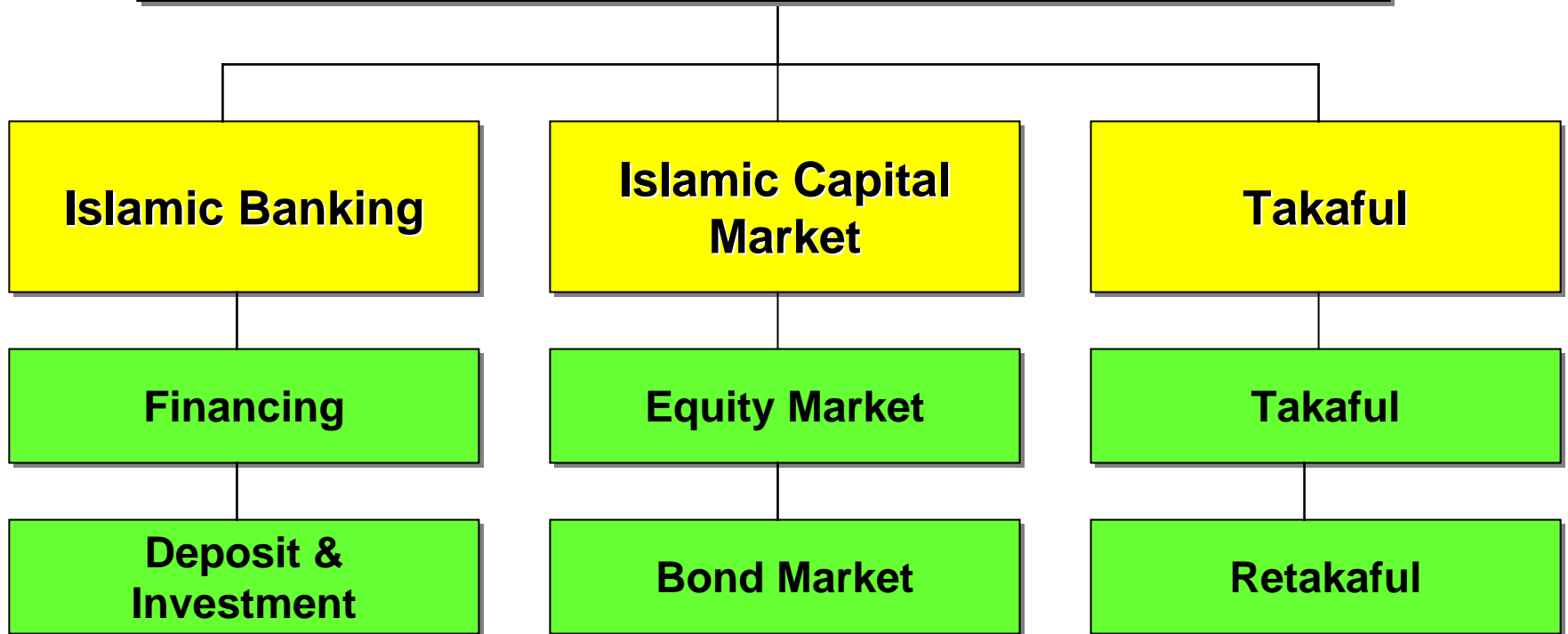




INTRODUCTION

- Shari`ah law works in financial transactions (mu`amalat) by way of interpretative efforts (ijtihad) of the primary sources (Quran & Sunnah); & using various secondary sources & techniques of arriving at legal rules
- Shari`ah law declares that the original status of each and every contract is permissibility unless proven otherwise (al-asl fi al`uqud al-ibahah)
- This doctrine of permissibility gives flexibility and opens up opportunities for innovation and creativity in “Islamic financial engineering” and product development

CONTEMPORARY ISLAMIC FINANCIAL SERVICES

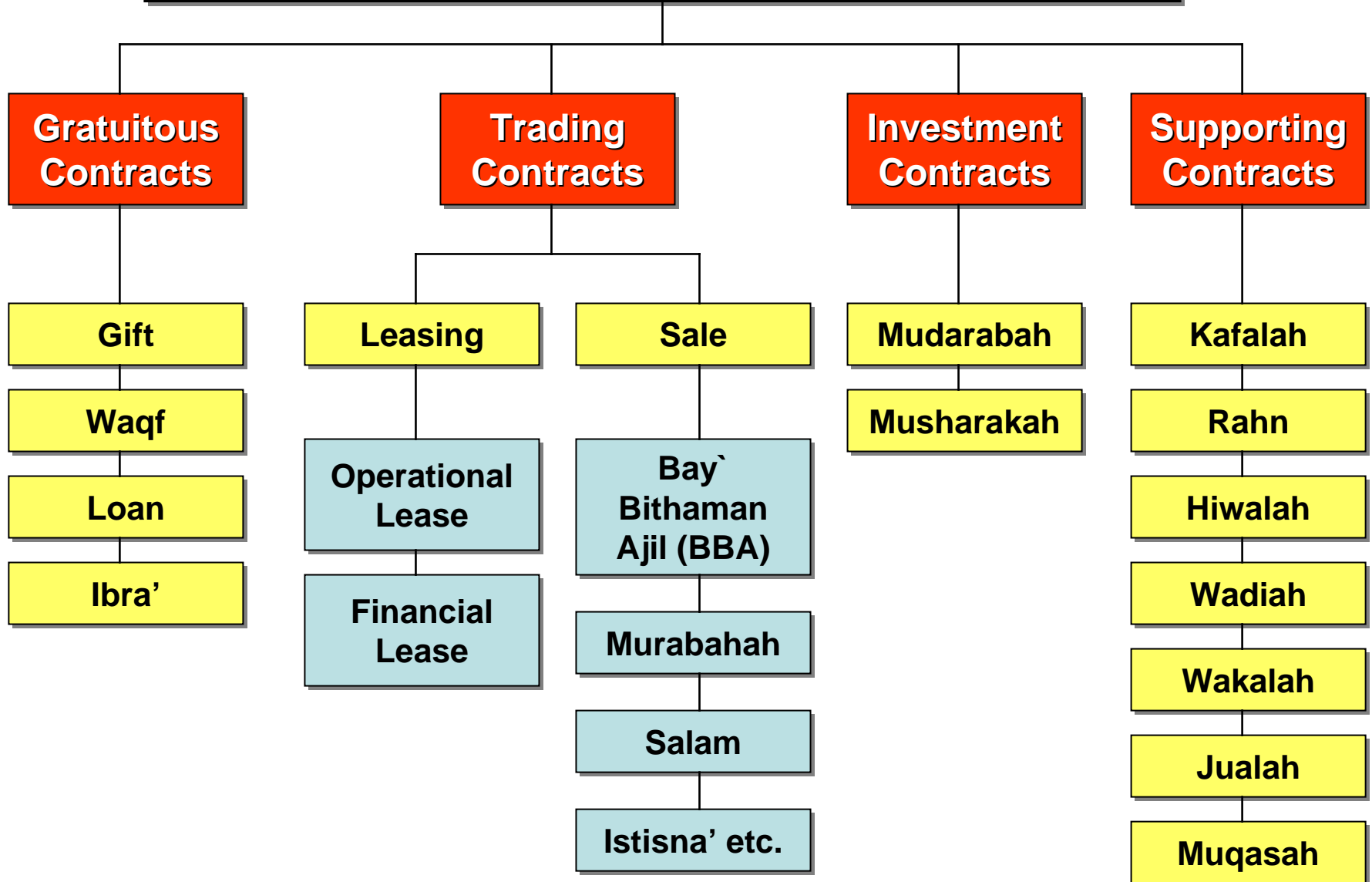


Bank Negara
IBA 1983 - Islamic Bank
BAFIA 1989 – Islamic
Windows

Securities Commission
SCA 1993
CA 1965

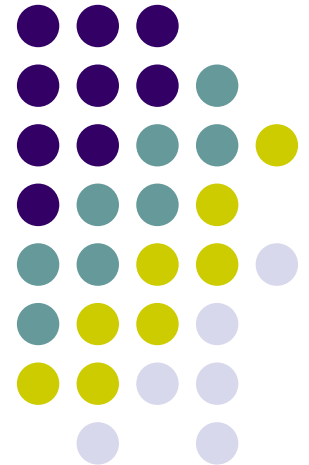
Bank Negara
Takaful Act 1984

KEY ISLAMIC COMMERCIAL CONTRACTS



SALE CONTRACTS & SOME APPLICATIONS IN ISLAMIC FINANCIAL SERVICES

- Murabahah & Bay` bithaman Ajil (BBA)
 - Application in Asset Financing
 - Application in Sukuk issuance



MURABAHAH & BAY` BITHAMAN AJIL (BBA)



- Both contracts are contracts of sale and purchase (bay`)
- Sale and purchase is a contract of exchange (`aqd al mu`awadah)
- The exchange is between the two counter values, i.e., goods and price
- Sale and purchase presupposes the transfer of ownership between the parties (regardless of any formal registration of transfer)

SPECIAL FEATURES FOR MURABAHAH & BAY` BITHAMAN AJIL (BBA)

Murabahah

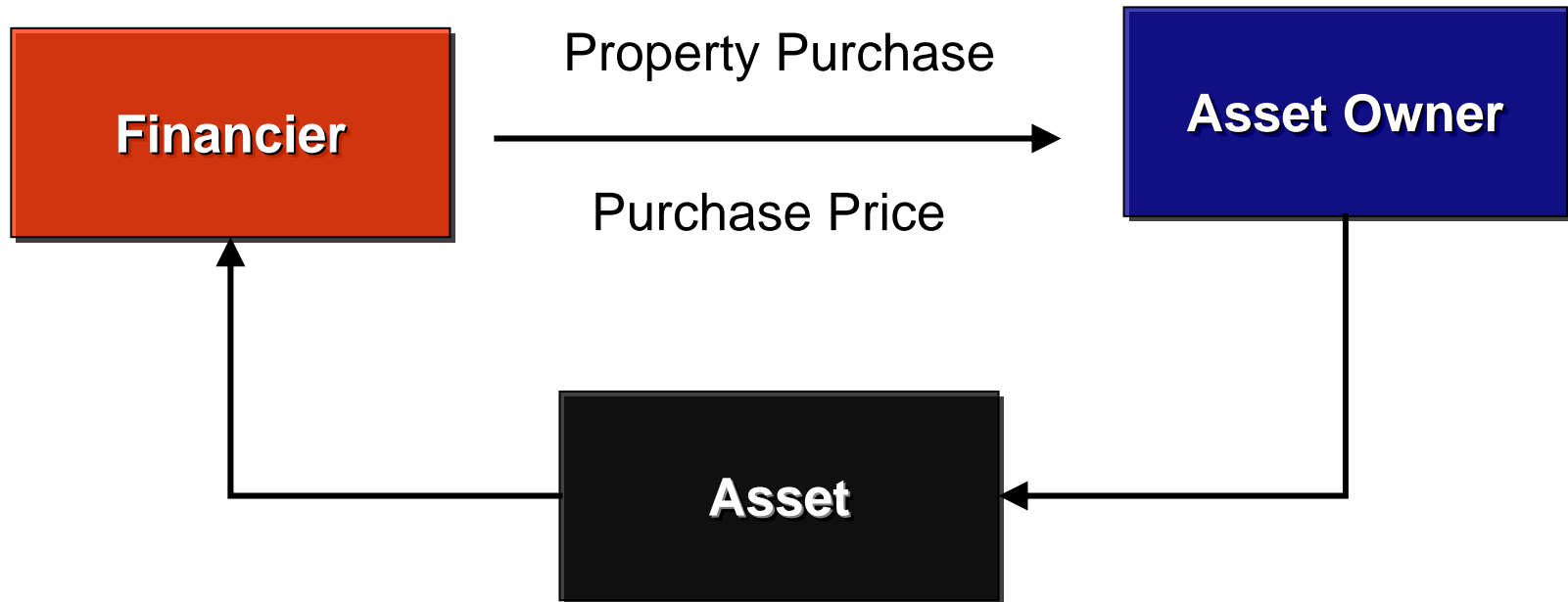
- It is a sale and purchase contract based on trust (bay` al amanah)
- Full disclosure and transparency between the parties
- Cost and amount of mark-up are disclosed
- Payment of price can be spot or deferred, depending on the agreement between the parties (if deferred – also a BBA)

BBA

- Sale where payment of price is deferred
- Final price should be contractually agreed and known to both parties
- Time and mode of payment should be ascertained
- No need to state the cost price and amount of mark-up (if disclosed – also a murabahah)

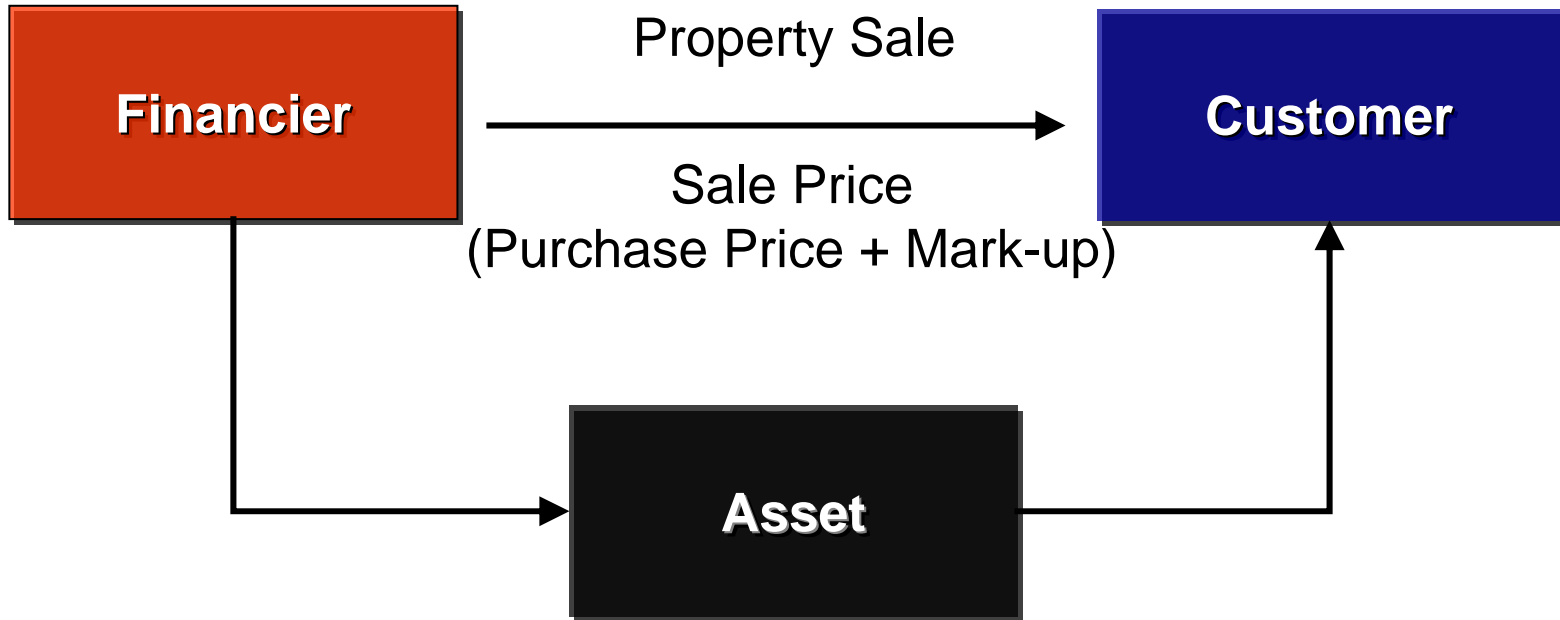
MURABAHAH & BBA

(Modus Operandi for Asset Financing)



STEP ONE

MURABAHAH & BBA (Modus Operandi for Asset Financing)



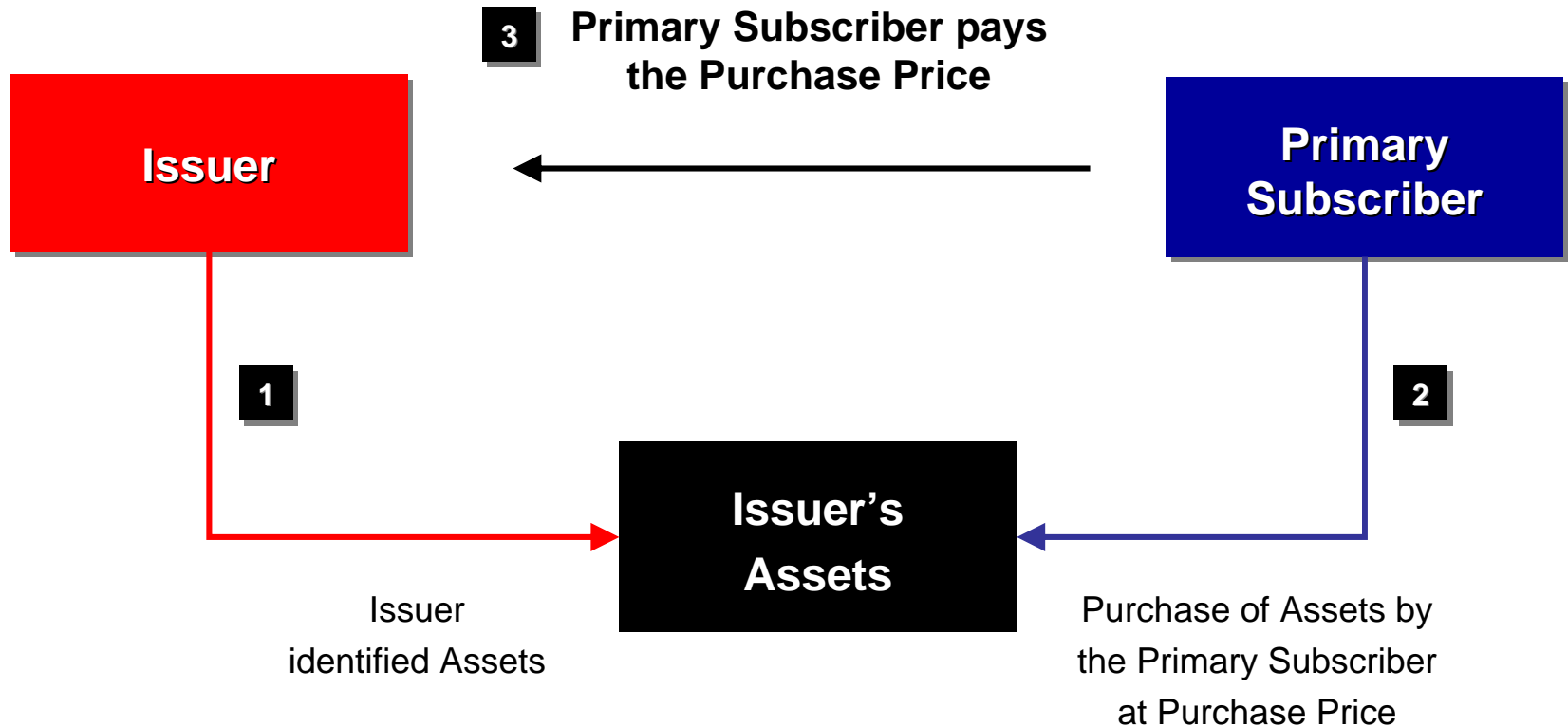
STEP TWO



OBSERVATIONS

- The Islamic banking practice in Malaysia tends to confine BBA to long term asset financing and Murabahah to short & medium term financing.
- This has nothing to do with any Islamic law requirement.
- BBA in Islamic law is simply a method of payment, i.e., “deferred payment” and thus, it applies to all kinds of sales where the payment is deferred whether on the basis of instalments or lump sum payment at the end of the tenor.

APPLICATION OF MURABAHAH/BBA IN SUKUK (BASIC STRUCTURE – MALAYSIA)



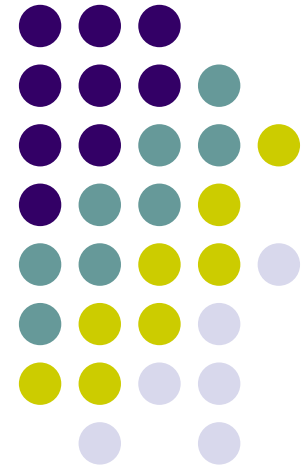
COMMENTS



- Murabahah/BBA sukuk are just tradable in Malaysian domestic market or perhaps some regional markets that adopt the Malaysian fatwa on bay` al `inah and bay` al dayn
- Not suitable for global / GCC market

IJARAH CONTRACT & SOME APPLICATIONS IN ISLAMIC FINANCIAL SERVICES

- Ijarah – Islamic lease
- Application of Ijarah as Operating Lease
- Application of Ijarah as Lease followed by Purchase (AITAB)
- Application of Ijarah in Sukuk Issuance

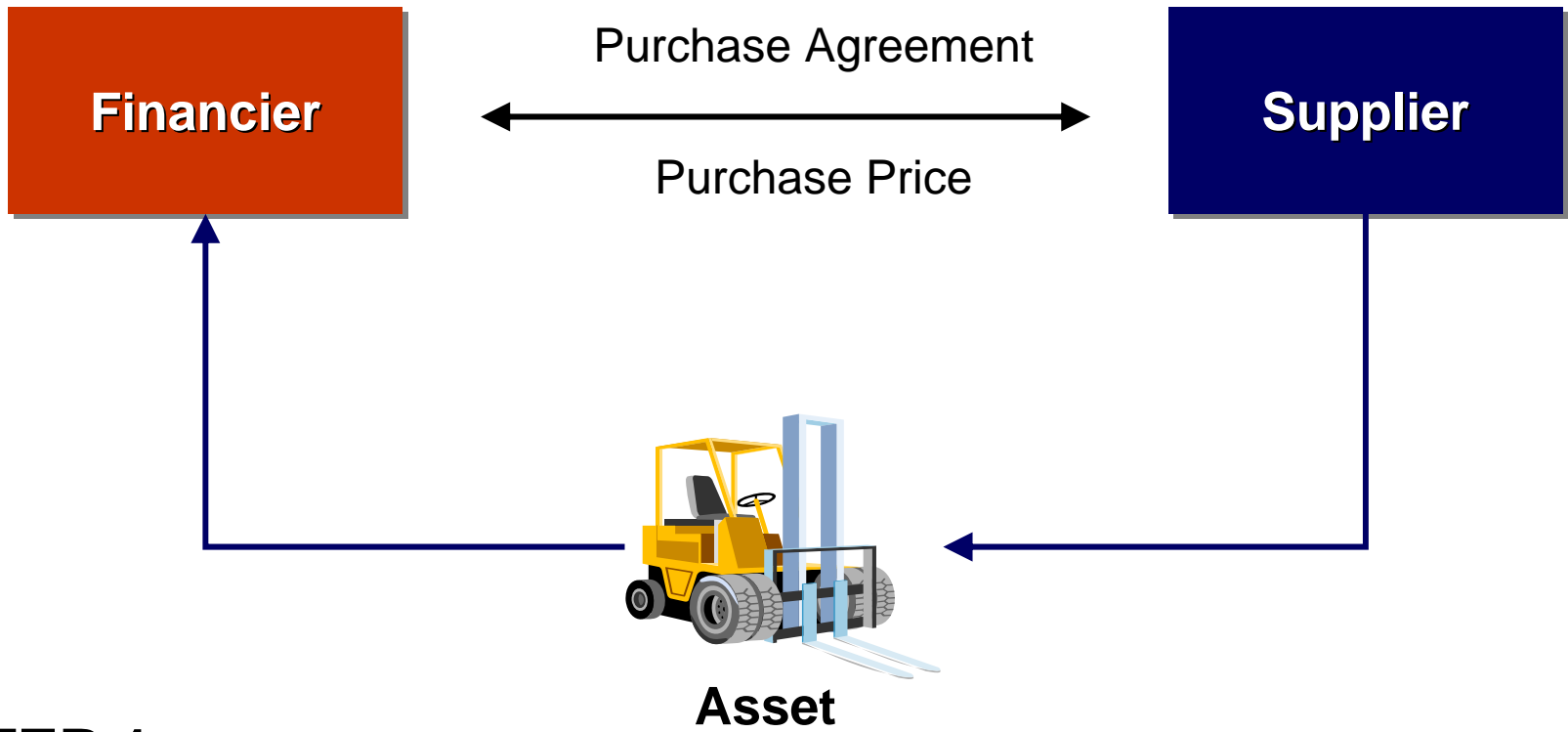




IJARAH – ISLAMIC LEASE

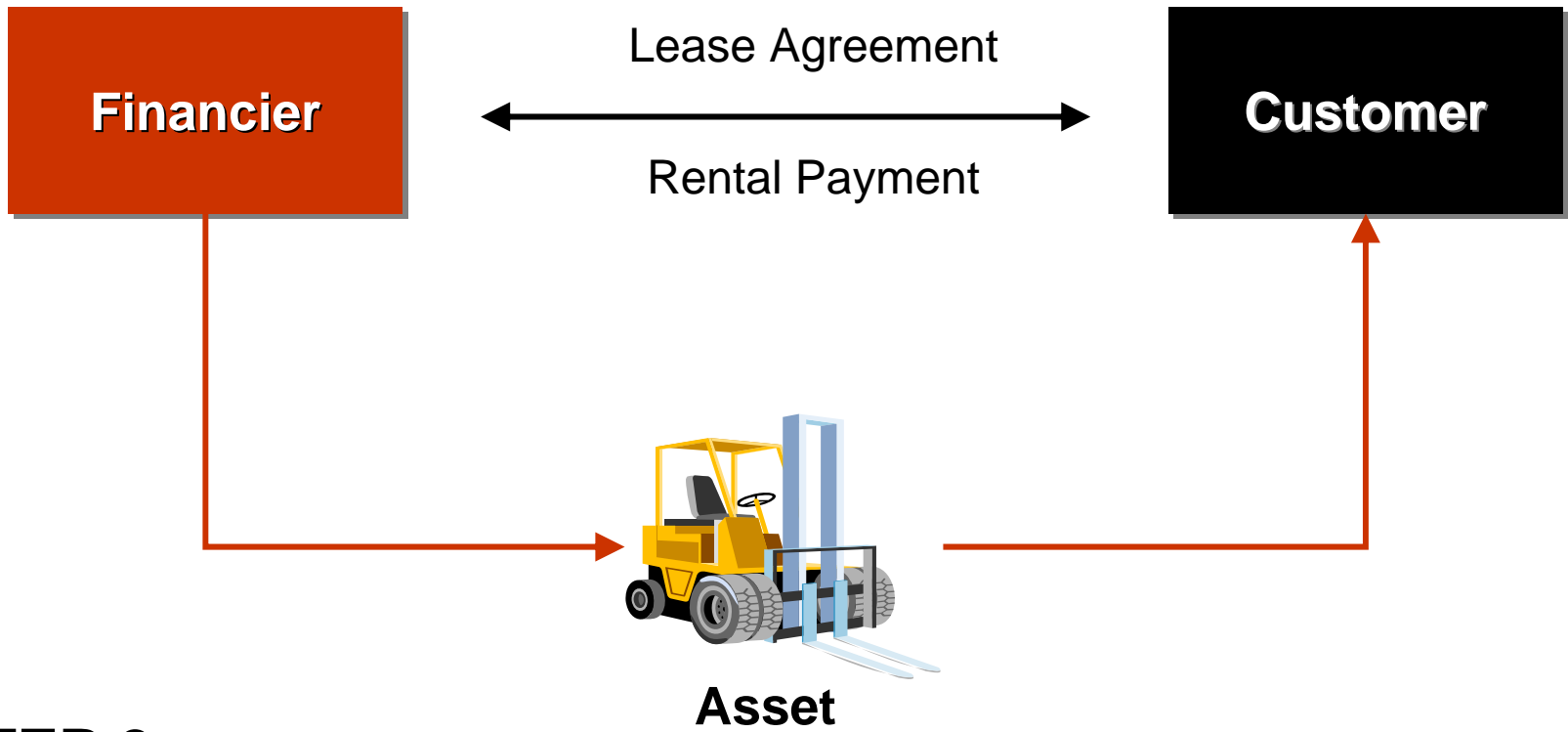
- Ijarah contract is a form of exchange contract (*`aqd al mu`awadah*) – usufruct vs rent.
- Ijarah is a contract that results in the transfer of the right to use (usufruct).
- The ownership of the asset remains with the owner cum lessor.
- In practice, ijarah can be used as operating lease or lease contract with an option to purchase – *al ijarah thumma al bay`* (AITAB).

OPERATING LEASE (Modus Operandi)



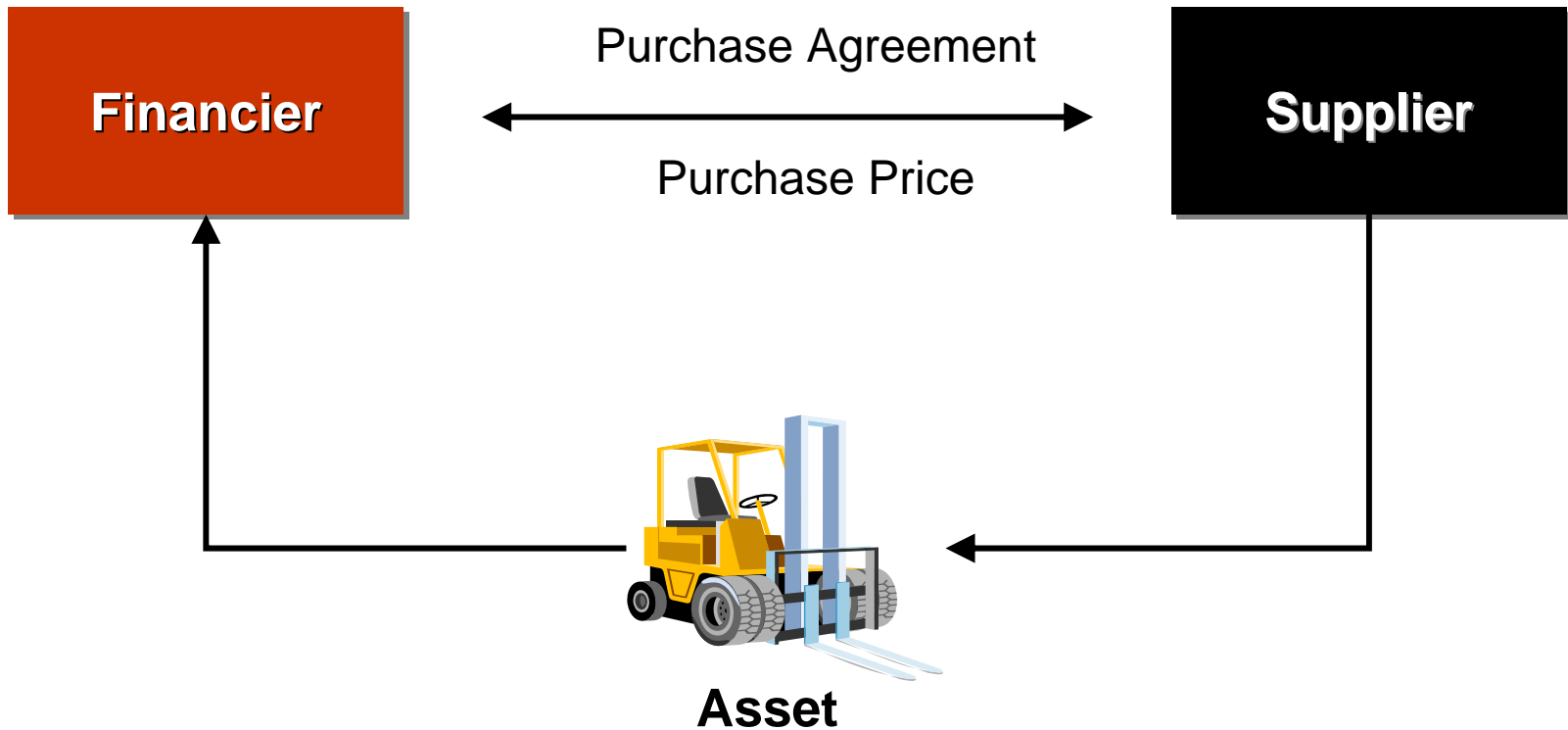
STEP 1

OPERATING LEASE (Modus Operandi)



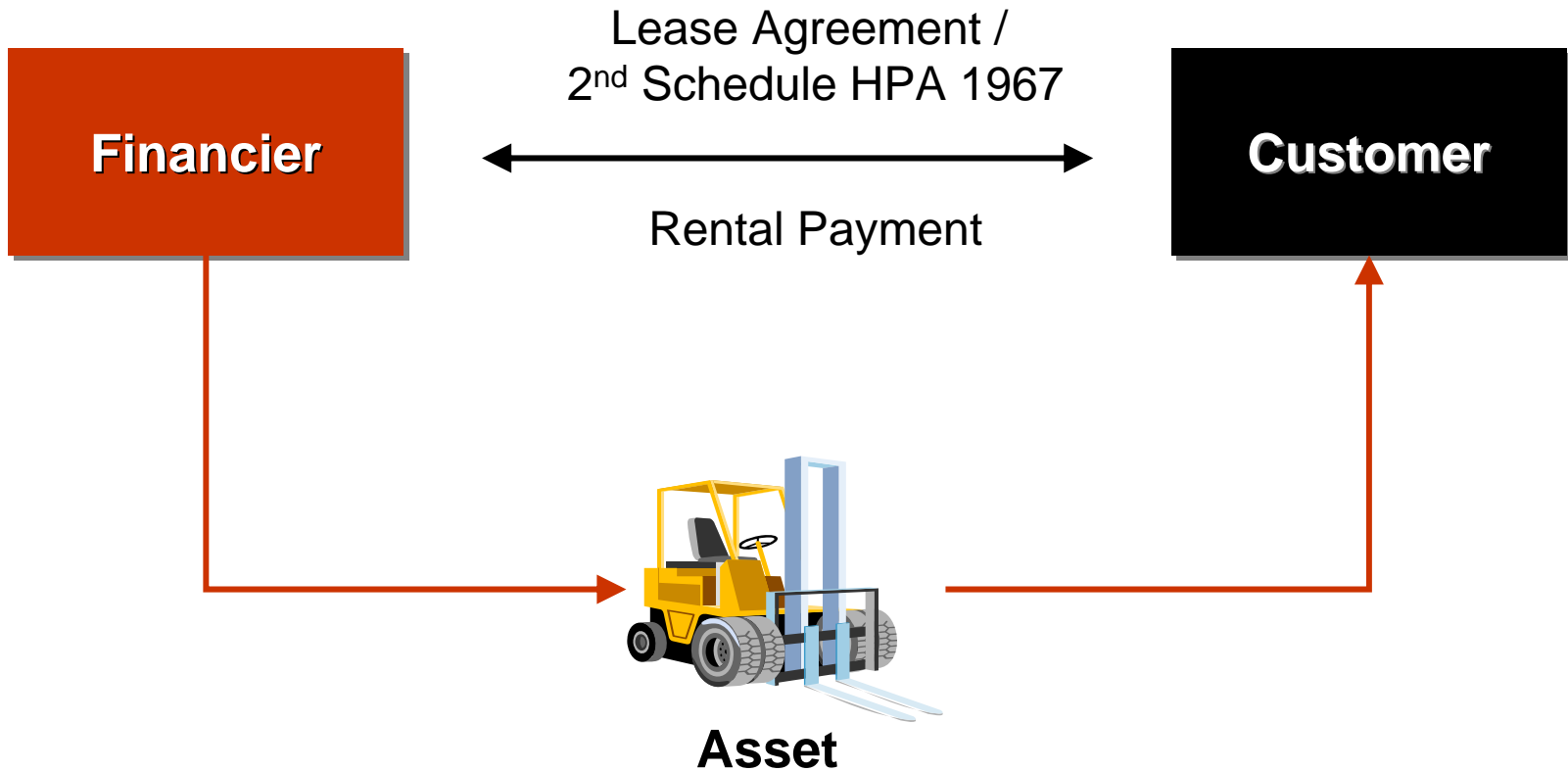
STEP 2

AL IJARAH THUMMA AL BAY' - AITAB (Modus Operandi)



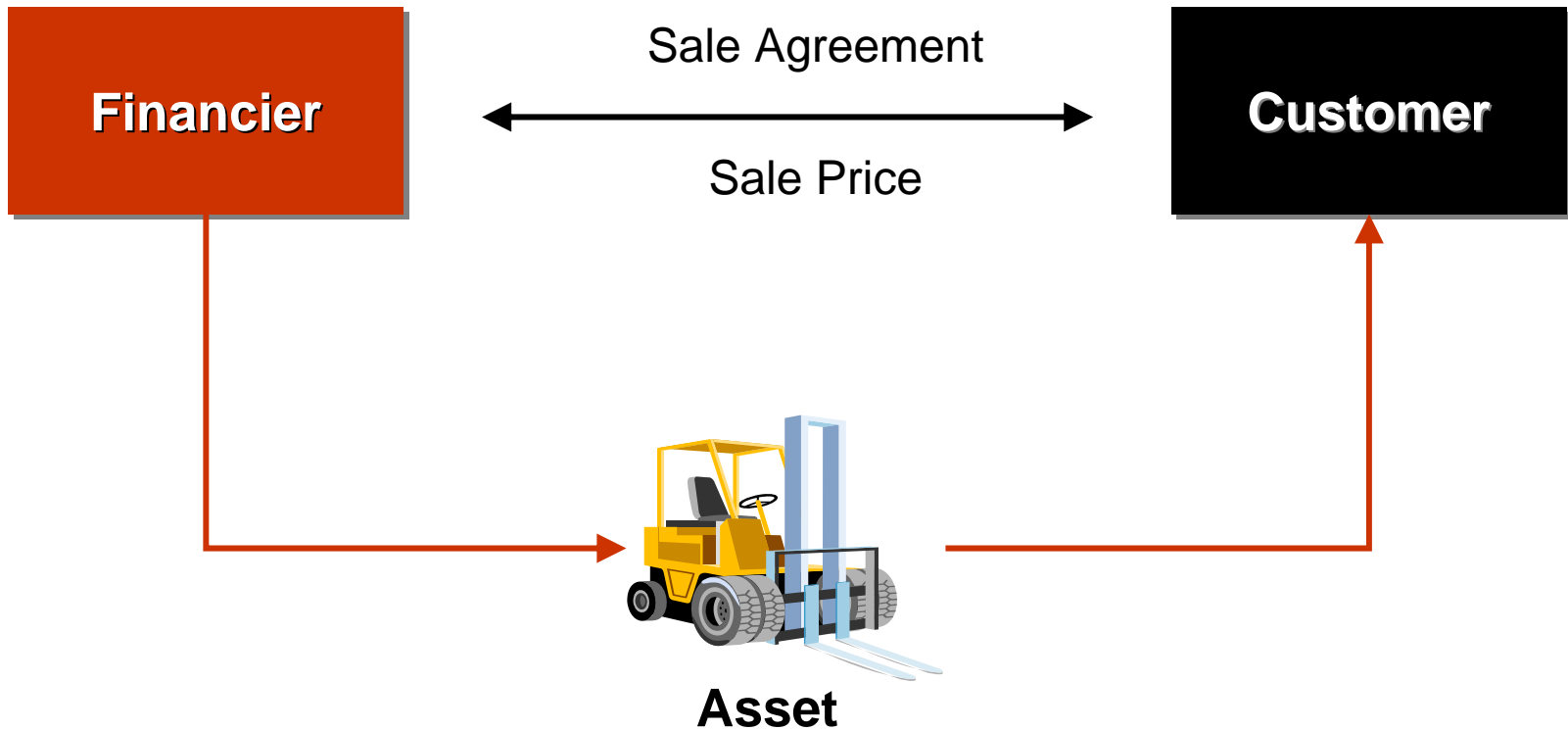
STEP 1

AL IJARAH THUMMA AL BAY' - AITAB (Modus Operandi)



STEP 2

AL IJARAH THUMMA AL BAY' - AITAB (Modus Operandi)



STEP 3

APPLICATION OF LEASE TO SUKUK (ISLAMIC SECURITIES)



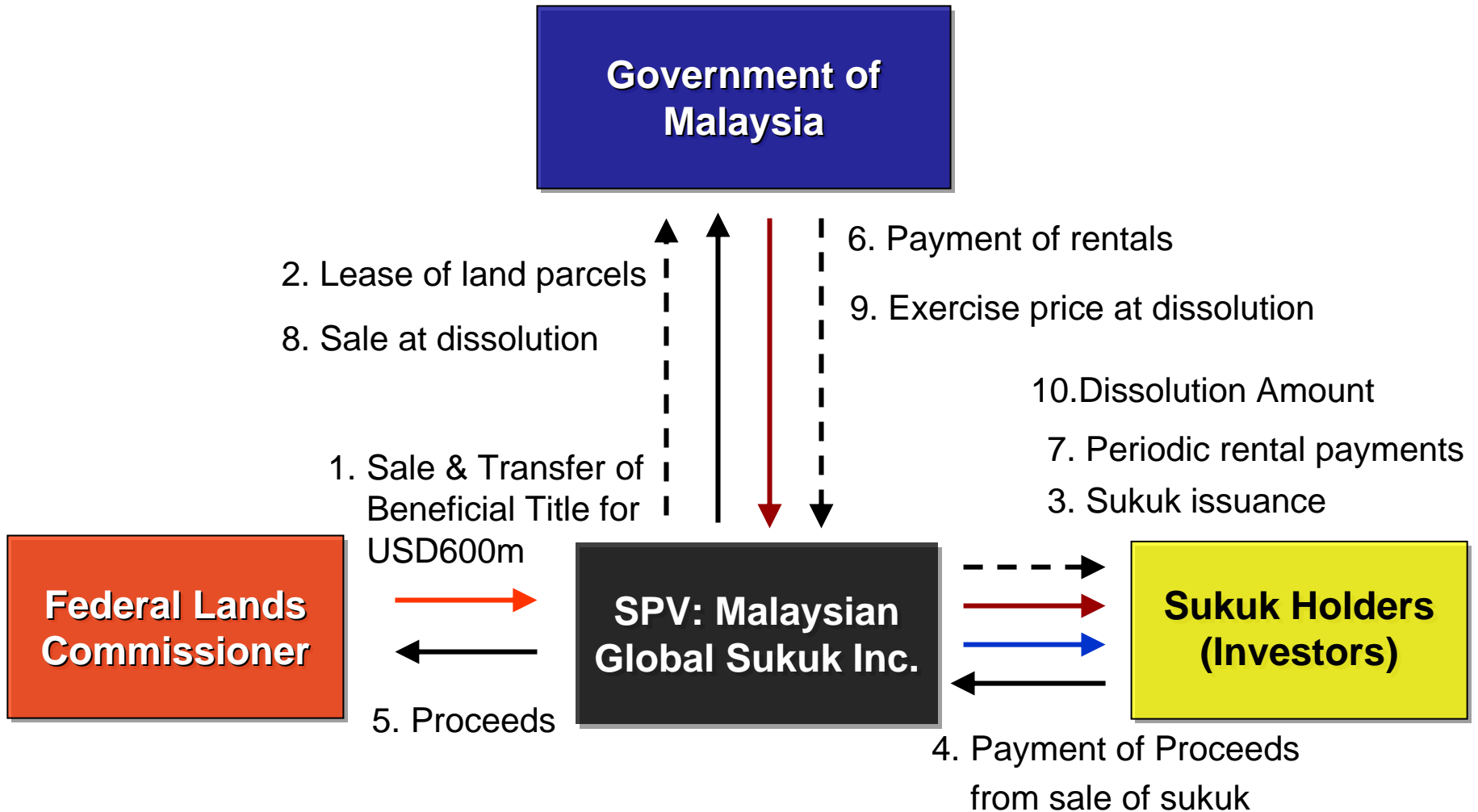
- Nature of Sukuk al Ijarah:
 - represents a share in a leased asset (pro-rata ownership by the sukuk holders of the leased asset)
 - share entitles to economic benefits under the lease (enables the sukuk holders to enjoy rental income & capital gain from disposal of the leased asset, if any)
 - subject to the obligations / liabilities (to bear the risk of loss and damage of the leased asset)

MALAYSIAN GLOBAL SOVEREIGN SUKUK: TRANSACTION SUMMARY



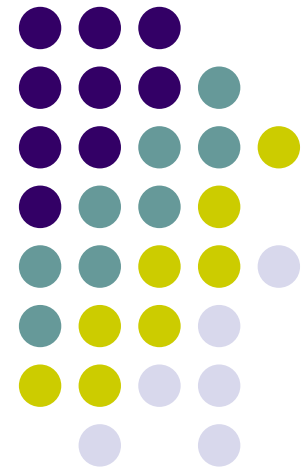
| | |
|-----------------------|---|
| Issuer | ● Malaysian Global Sukuk Inc. |
| Rating | ● Baa2 (Moody's) and BBB (S&P) |
| Size | ● USD 600 million |
| Format | ● Reg-S |
| Type | ● Sukuk al Ijarah (floating rate) |
| Tenor | ● 5 year bullet |
| Yield & Coupon | ● USD LIBOR + 95 bps |
| Listing | ● Bahrain, Luxembourg & Labuan (LFX) |
| Launch/Pricing Date | ● June 2002 |
| Investor Distribution | ● 51% Mid-East; 30% Asia; 15% Europe; 4% US |

USD600m MALAYSIAN GLOBAL SOVEREIGN SUKUK: TRANSACTION STRUCTURE



PARTNERSHIP CONTRACTS & SOME APPLICATIONS IN ISLAMIC FINANCIAL SERVICES

- Application of Musharakah in Project Financing
 - Musharakah
- Application of Mudarabah in Project Financing
 - Mudarabah
- Application of Musharakah & Mudarabah in Sukuk Issuance

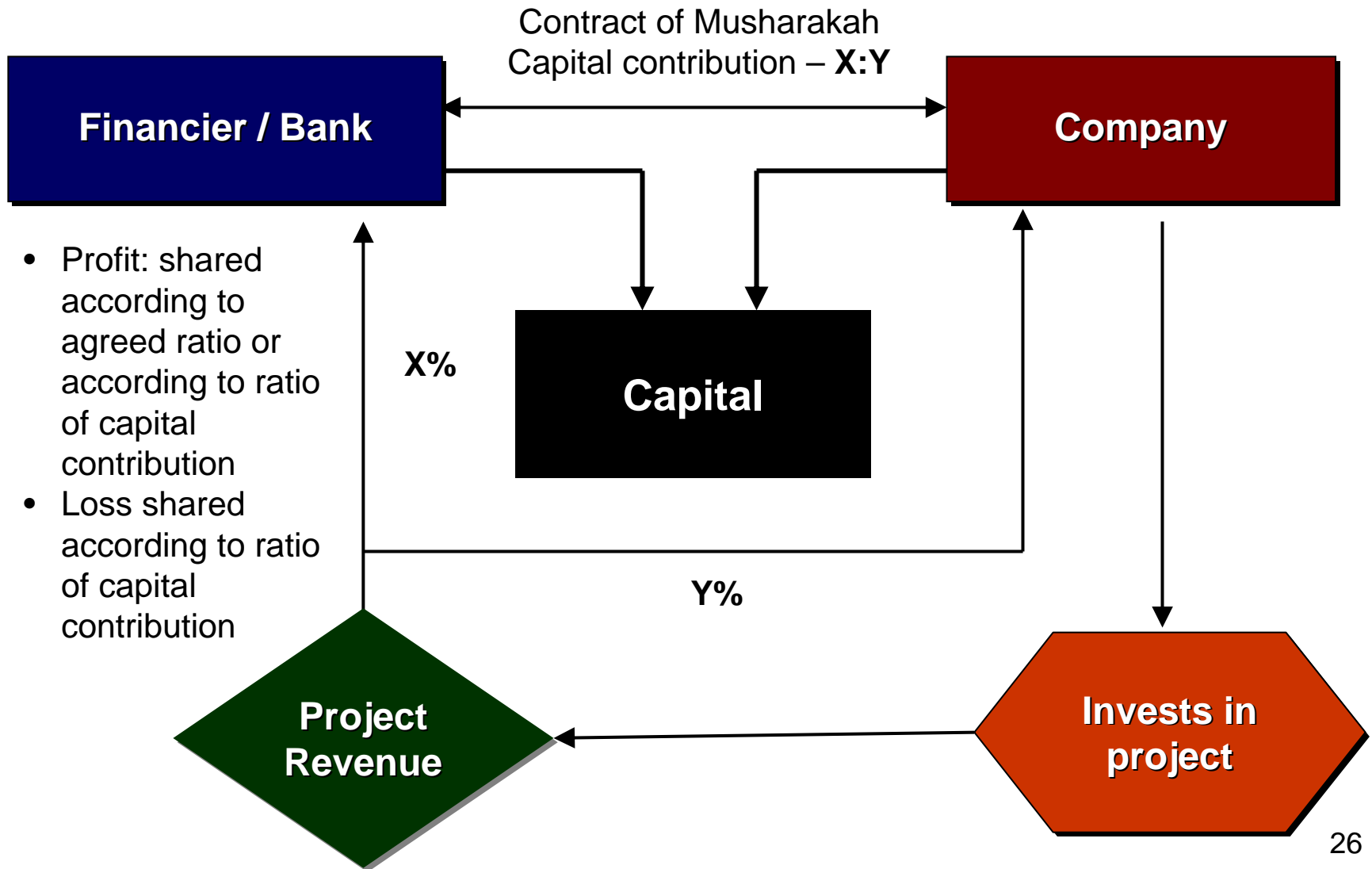


MUSHARAKAH



- Meaning of “*musharakah*”:
 - “an arrangement whereby two or more persons contribute to the capital with their property for the purpose of trading with the joint capital, the profit of which, shall be shared among the partners”

MUSHARAKAH PROJECT FINANCING

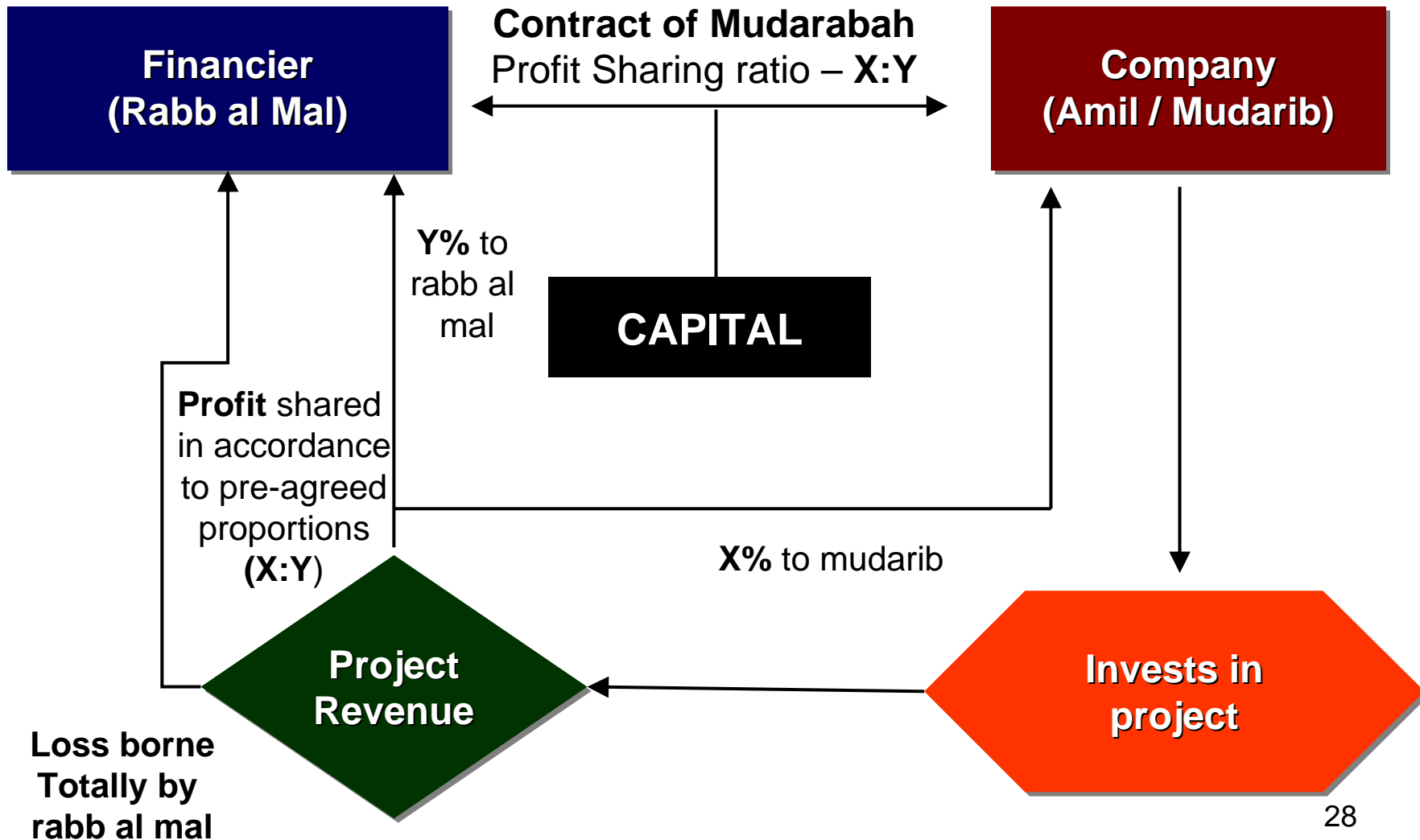


MUDARABAH

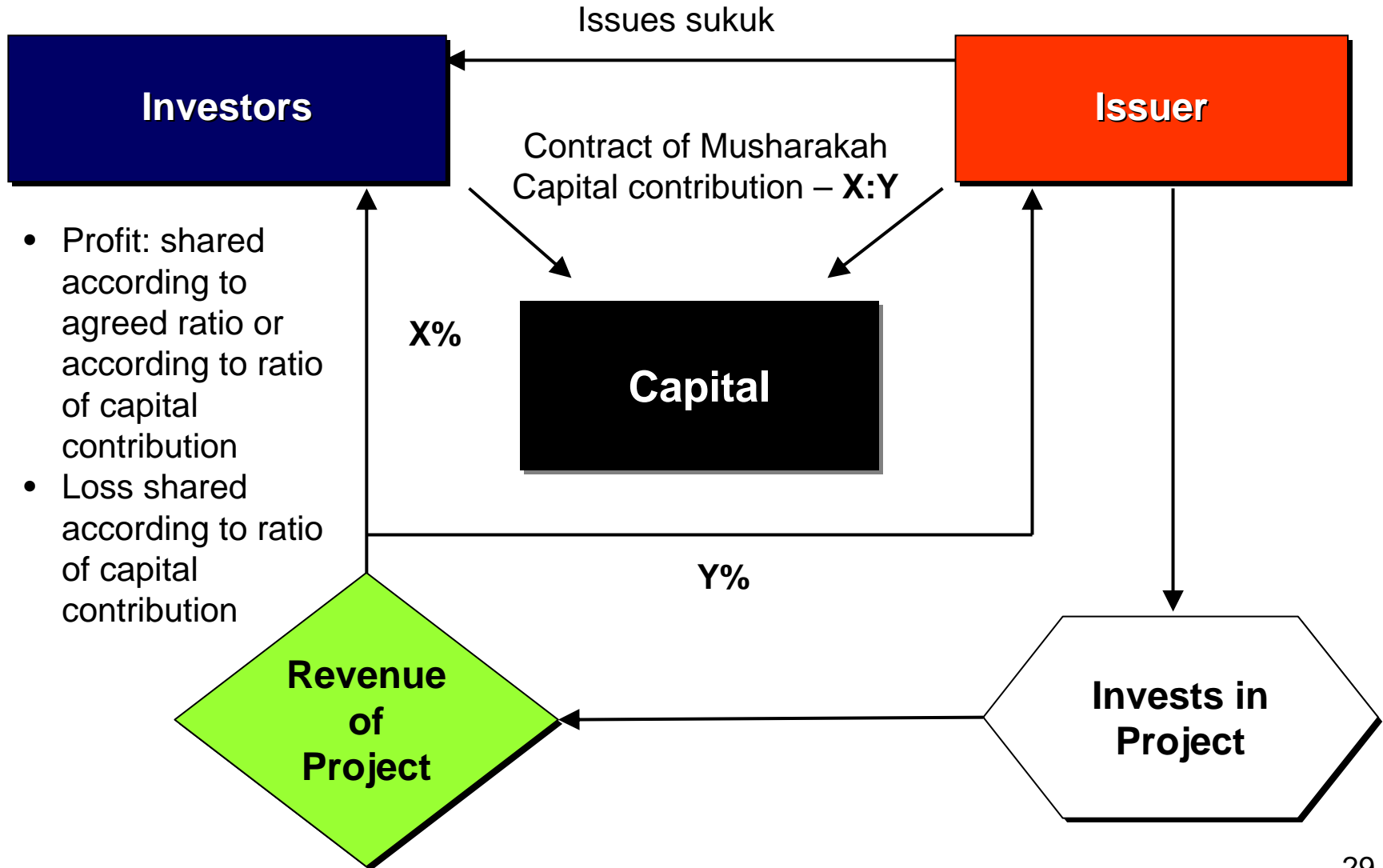


- Meaning of *mudarabah*:
 - “an arrangement whereby the owner of some property (termed as *rabb al mal*) gives a specified amount of capital to another person (termed as *mudarib*) who is to act as the entrepreneur to trade with the capital, the profit of which will be shared between the two parties according to the terms of their agreement. The losses will be borne by the *rabb al mal* as the financier, whilst the *mudarib* suffers the frustration of a fruitless effort”

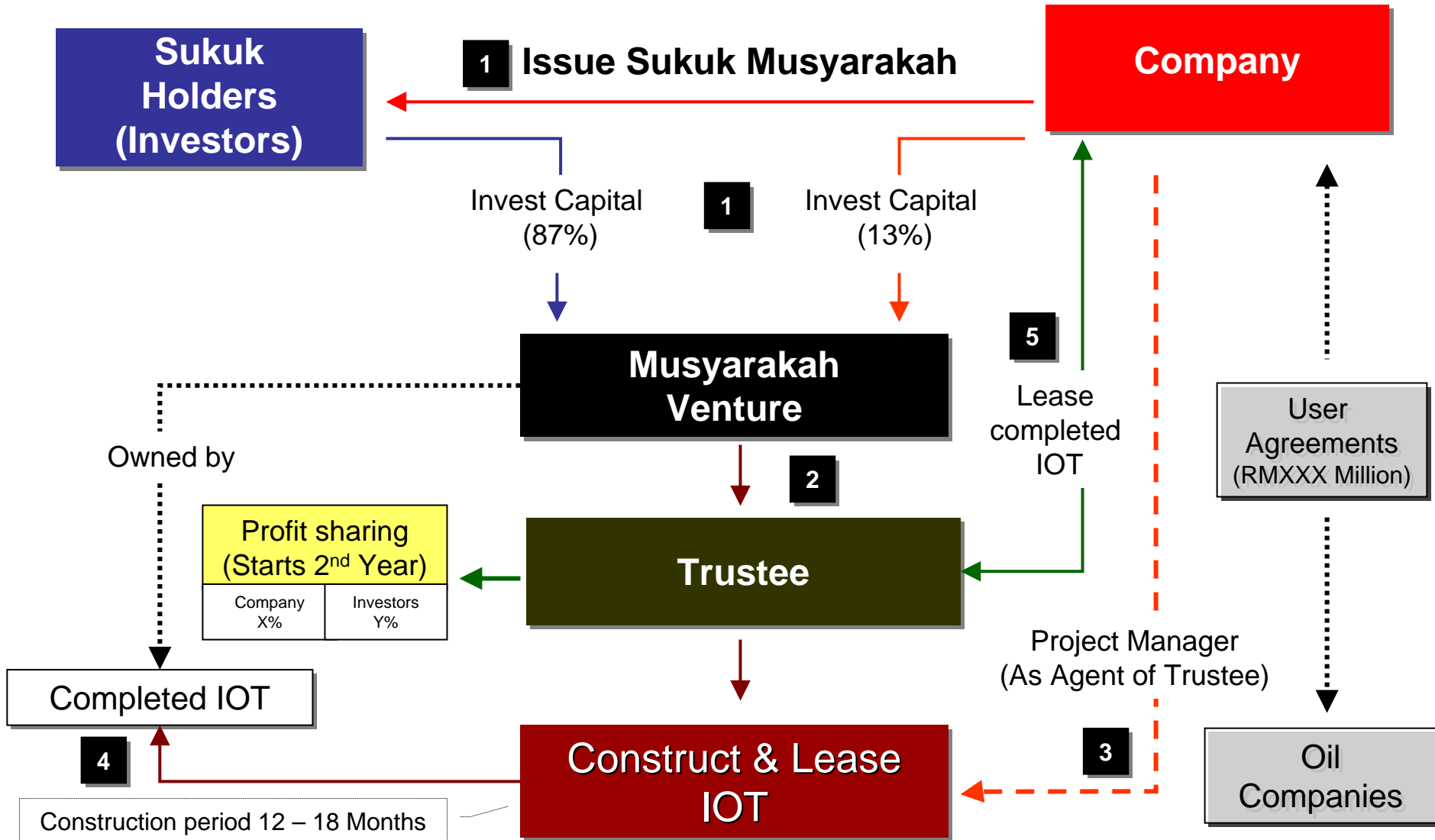
MUDARABAH PROJECT FINANCING



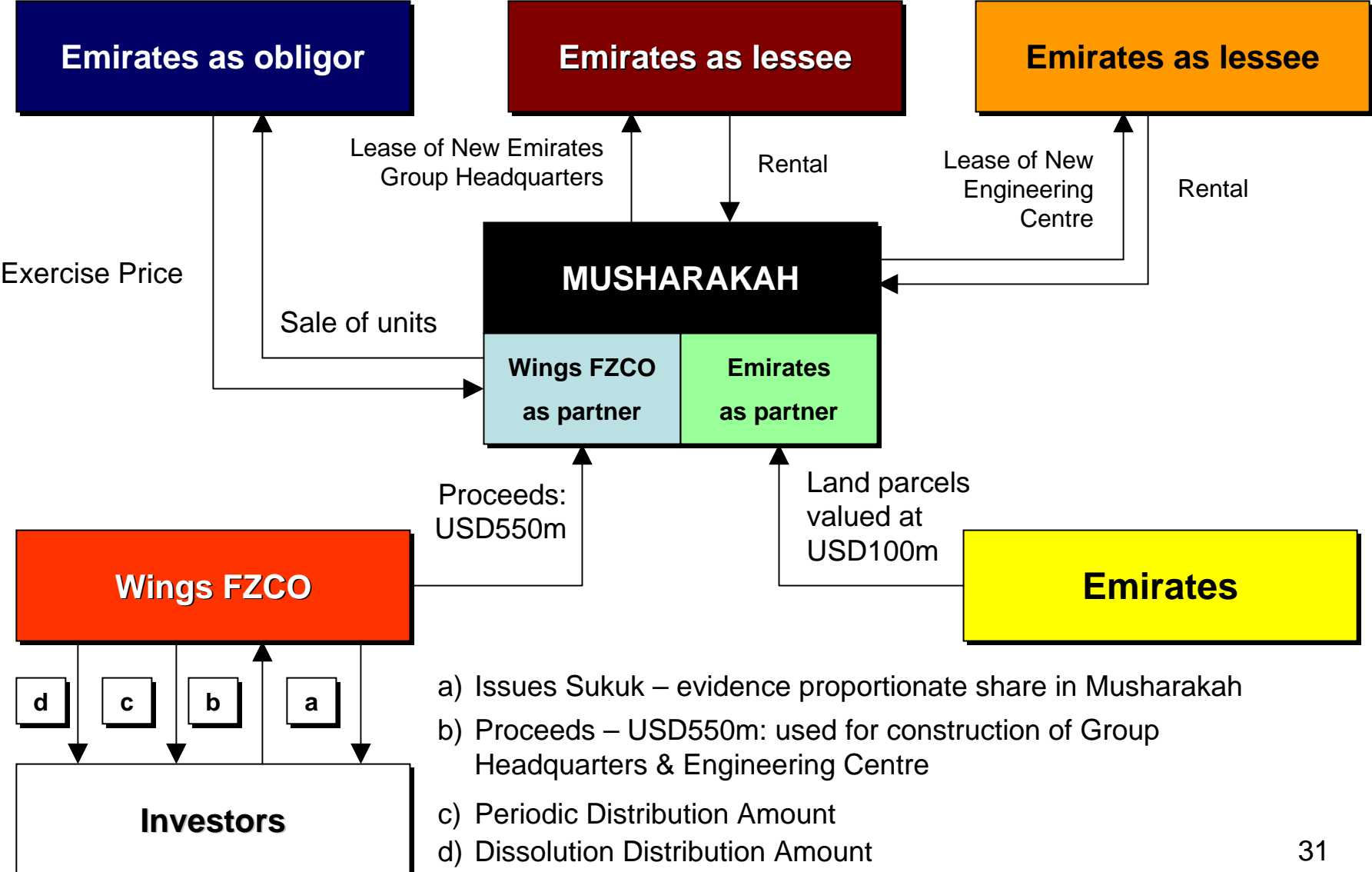
BASIC STRUCTURE OF MUSHARAKAH SUKUK



ASSAR SENARI RM150m MUSHARAKAH SUKUK: TRANSACTION STRUCTURE

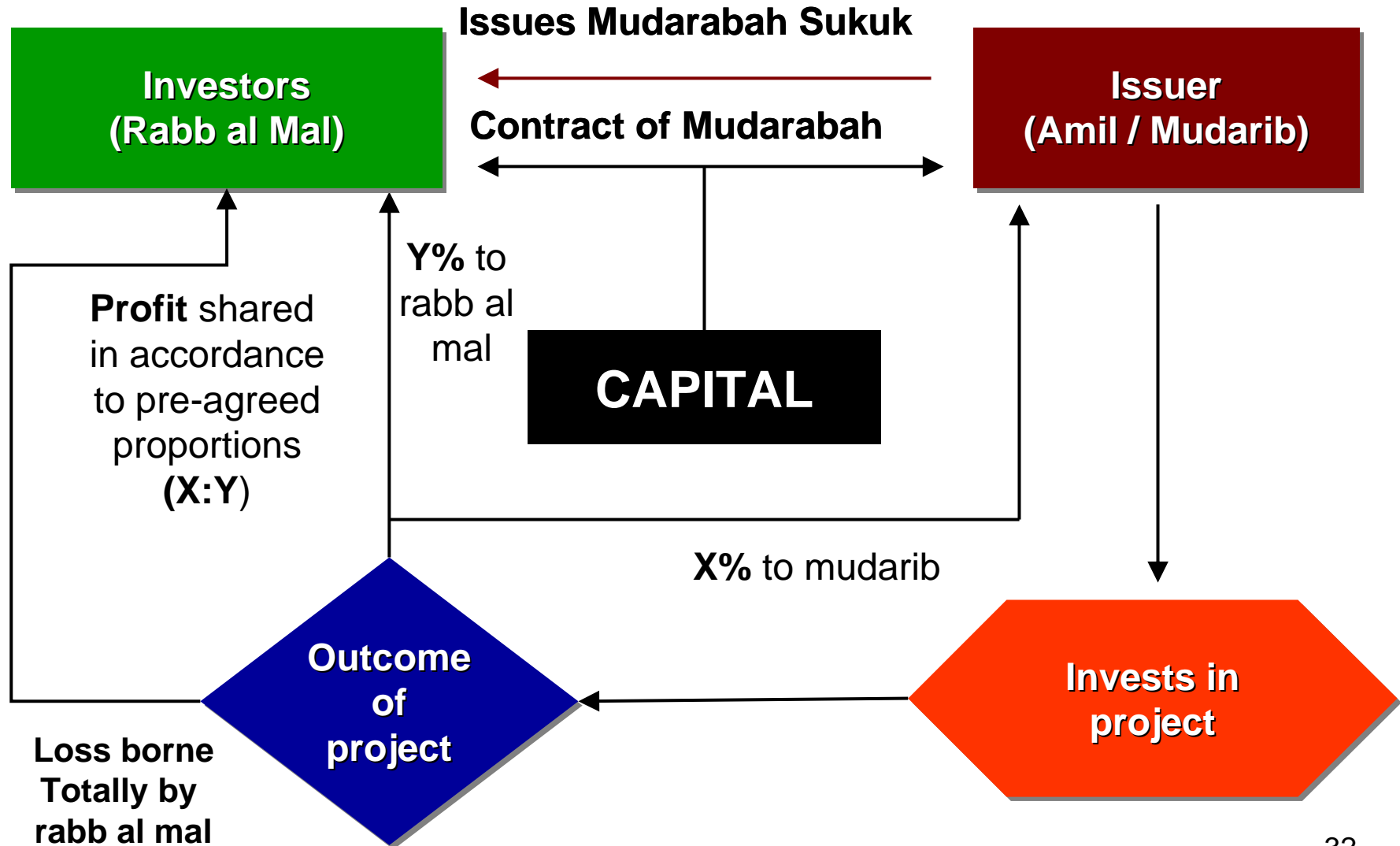


WINGS FZCO: TRANSACTION STRUCTURE

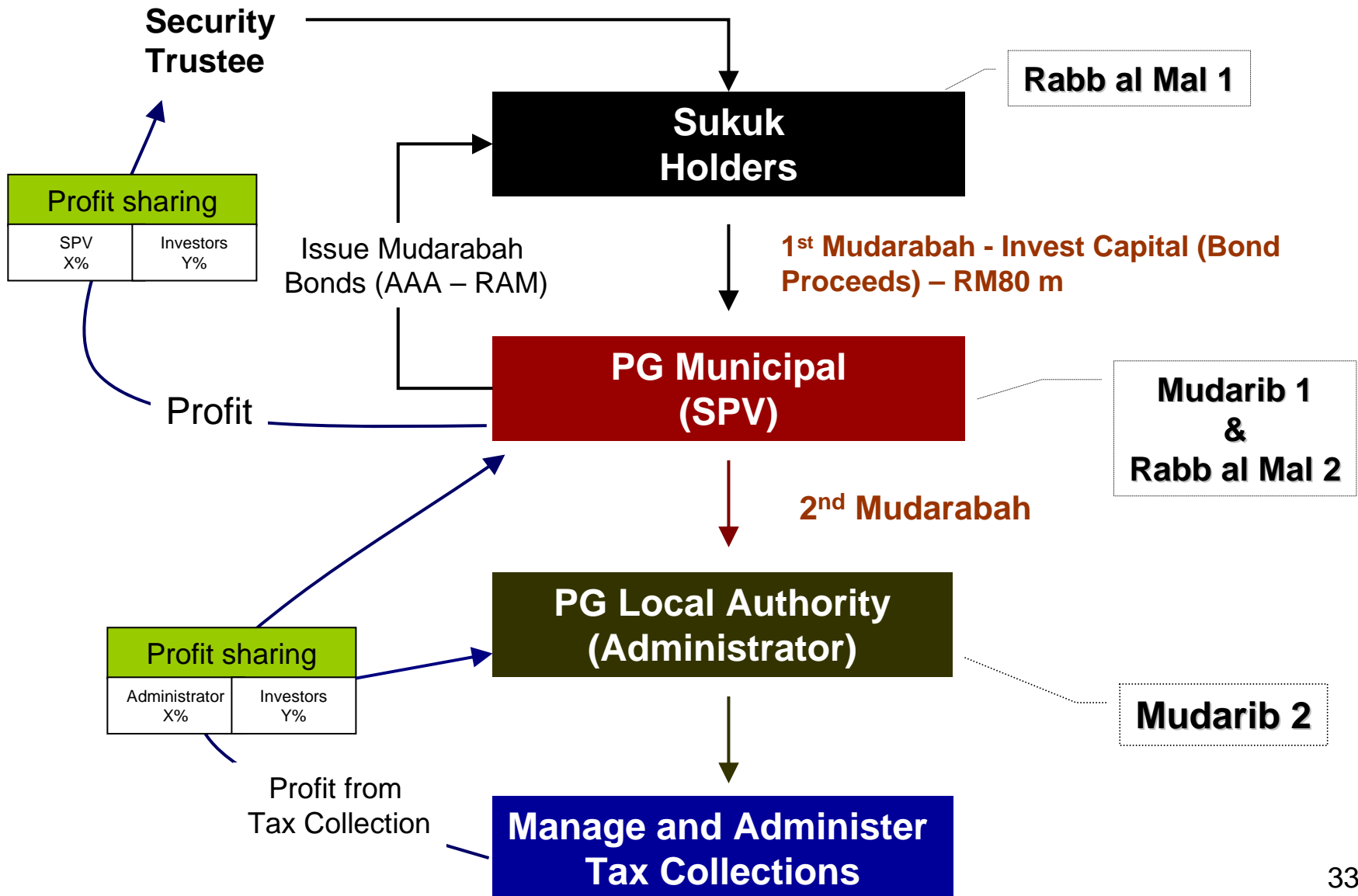


- a) Issues Sukuk – evidence proportionate share in Musharakah
- b) Proceeds – USD550m: used for construction of Group Headquarters & Engineering Centre
- c) Periodic Distribution Amount
- d) Dissolution Distribution Amount

BASIC STRUCTURE OF MUDARABAH SUKUK

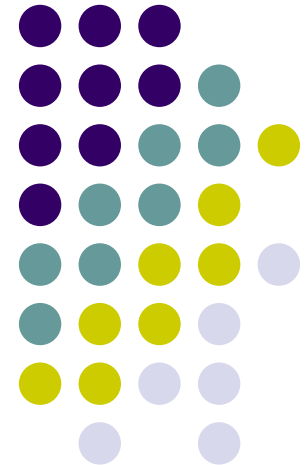


PG MUNICIPAL MUDARABAH SUKUK

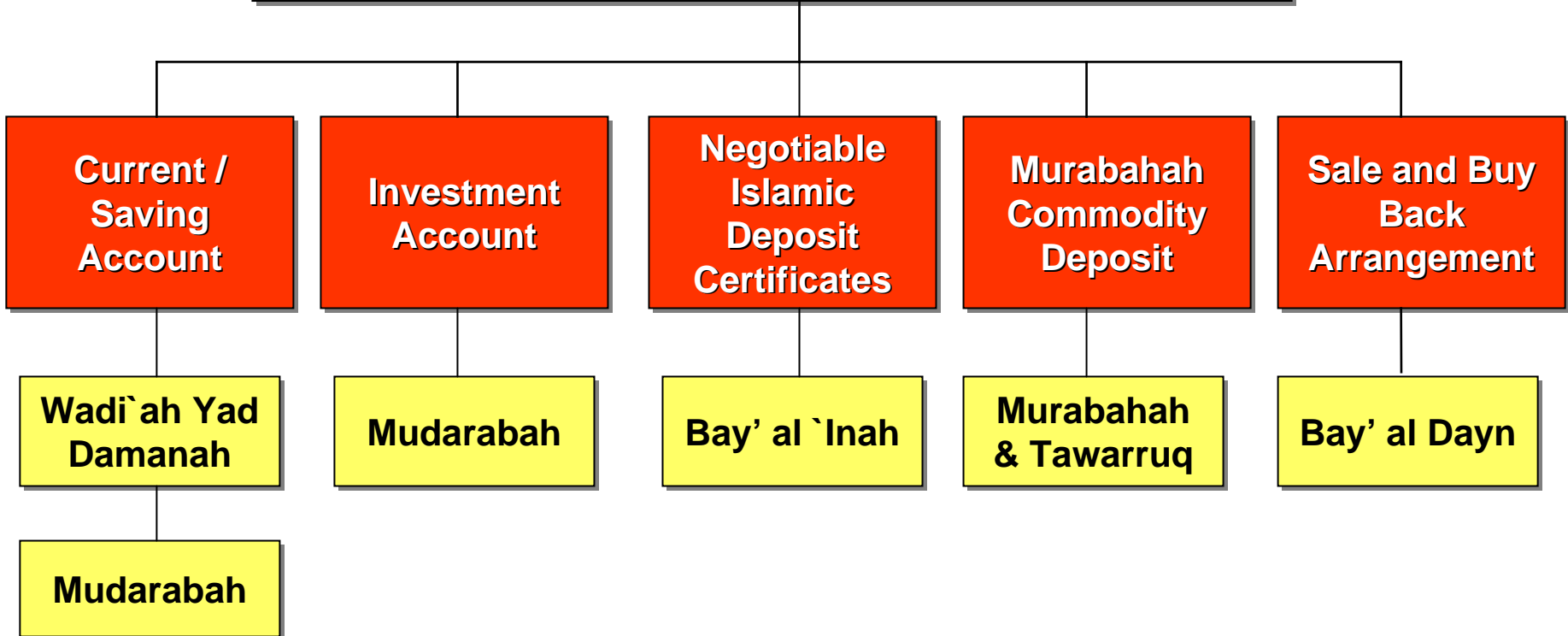


ISLAMIC DEPOSIT SERVICES PRODUCTS: SOME APPLICATIONS

- Islamic Deposit Services Products
- Islamic Savings / Current Account – Wadi`ah
 - Islamic Accounts – Mudarabah
 - Islamic Deposits – NIDC
- Islamic Deposits – Murabahah Commodity



DEPOSIT SERVICES PRODUCTS



ISLAMIC SAVING & CURRENT ACCOUNTS



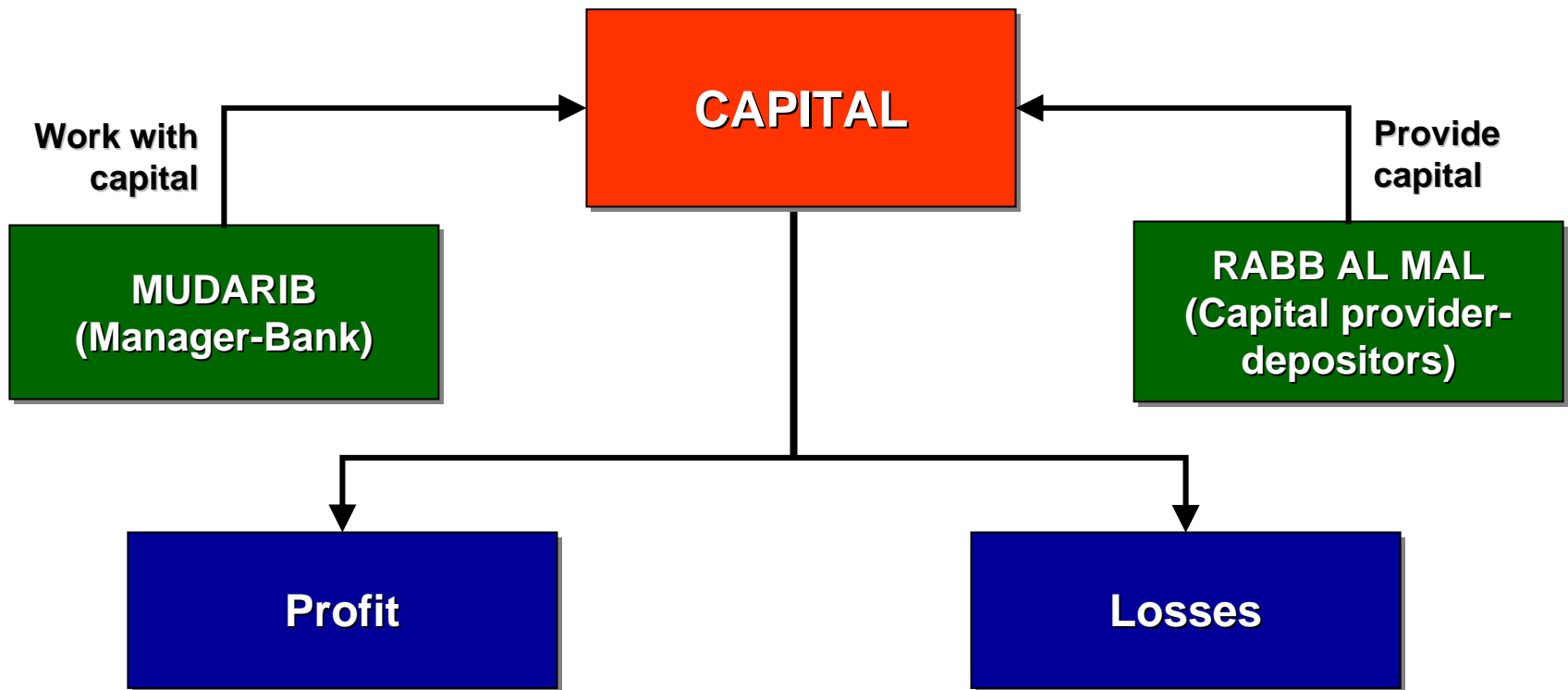
- Some Islamic banks use the concept of wadi`ah yad damanah (guaranteed safe custody) in their Islamic saving & current account
- Other Islamic banks use mudarabah contracts for Islamic savings & current accounts
- For Islamic investment accounts – normally mudarabah contract is used.

FEATURES OF WADI`AH YAD DAMANAH (GUARANTEED SAFE CUSTODY)



- The custodian (bank) is both a trustee and guarantor
- The deposit need not be separated/segregated
- The deposit can be used for trading, etc.
- The custodian (bank) has a right to any income derived from the utilization of the deposit
- Depositor can take back the deposited asset at any time
- Wadi'ah Yad Damanah is more like Qard (loan); thus, all principles of loan would be applicable
- Wadi`ah Yad Damanah (like loan) cannot generate any pre-agreed benefit/income to the depositor, over and above the principal amount of deposit. Failure to safeguard this may result in riba

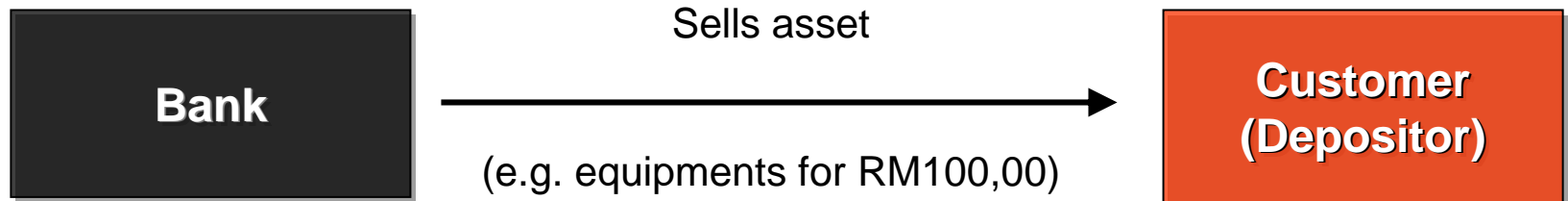
MUDARABAH ACCOUNT (MODUS OPERANDI)



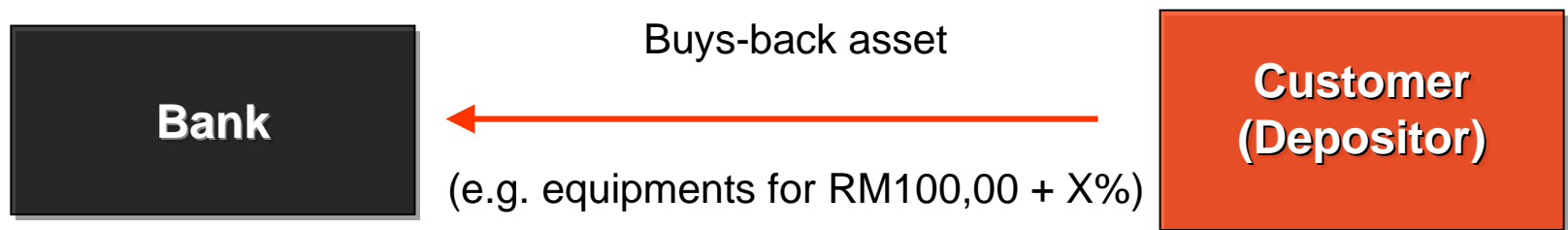
- Shared between mudarib + rabb al mal
- Profit sharing according to a contractually agreed ratio
- Profit sharing cannot be a fixed amount/a fixed percentage of capital contribution

- Born solely by rabb al mal
- Mudarib will only be personally liable if the loss is caused by his negligence

NIDC (MODUS OPERANDI)



Method of payment: cash – “Islamic Deposit”

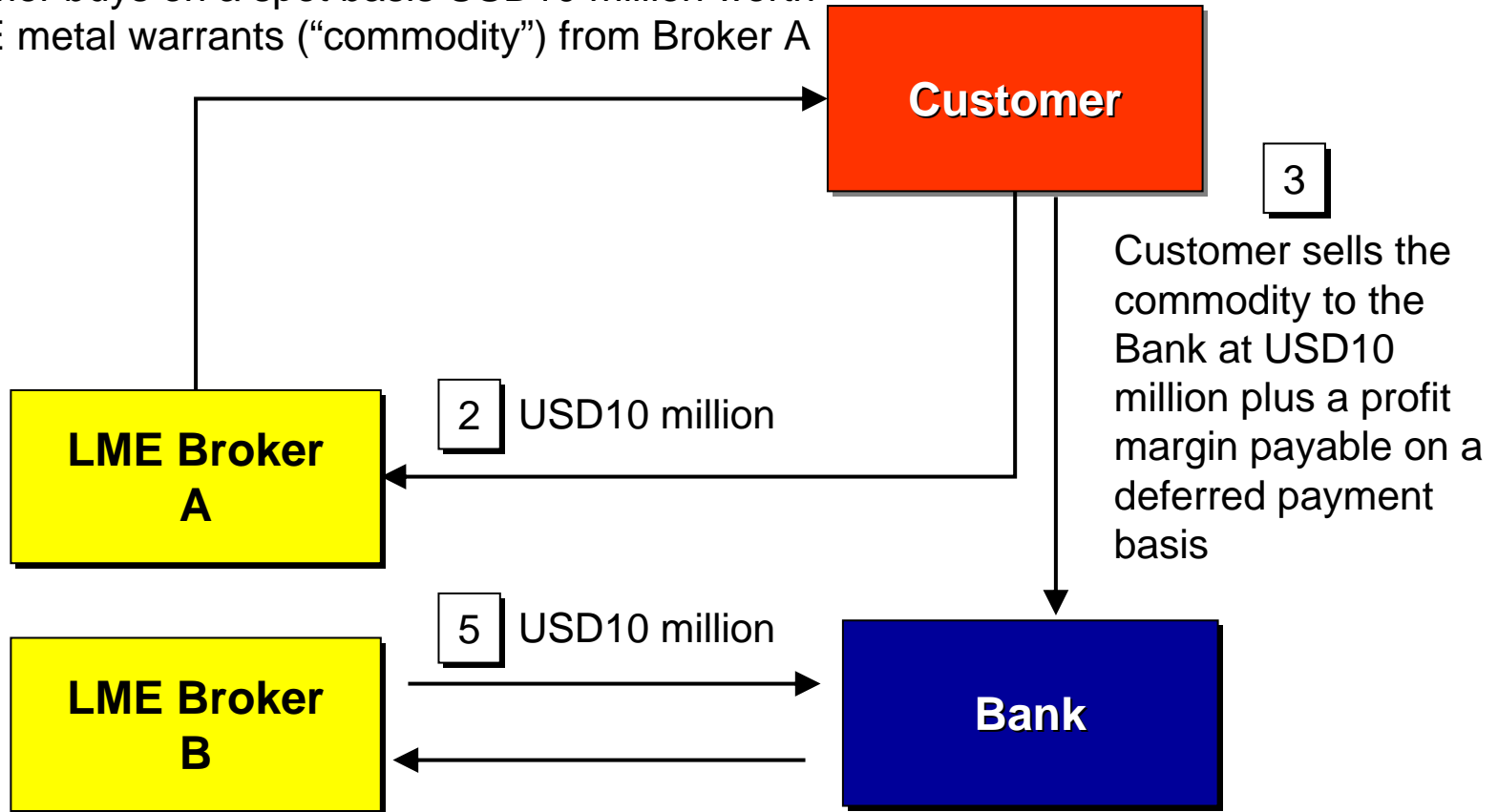


Method of payment: deferred over a period of 5 years Bank also issues NIDC to evidence the indebtedness created by the deferred payment sale

MURABAHAH COMMODITY DEPOSIT-I

1

Customer buys on a spot basis USD10 million worth of LME metal warrants (“commodity”) from Broker A



3

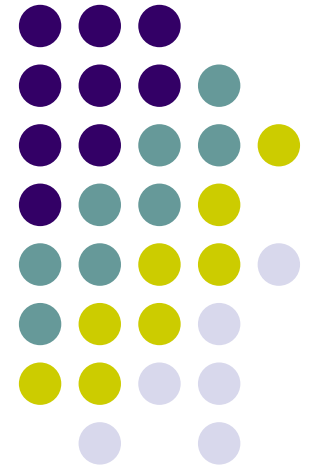
Customer sells the commodity to the Bank at USD10 million plus a profit margin payable on a deferred payment basis

4

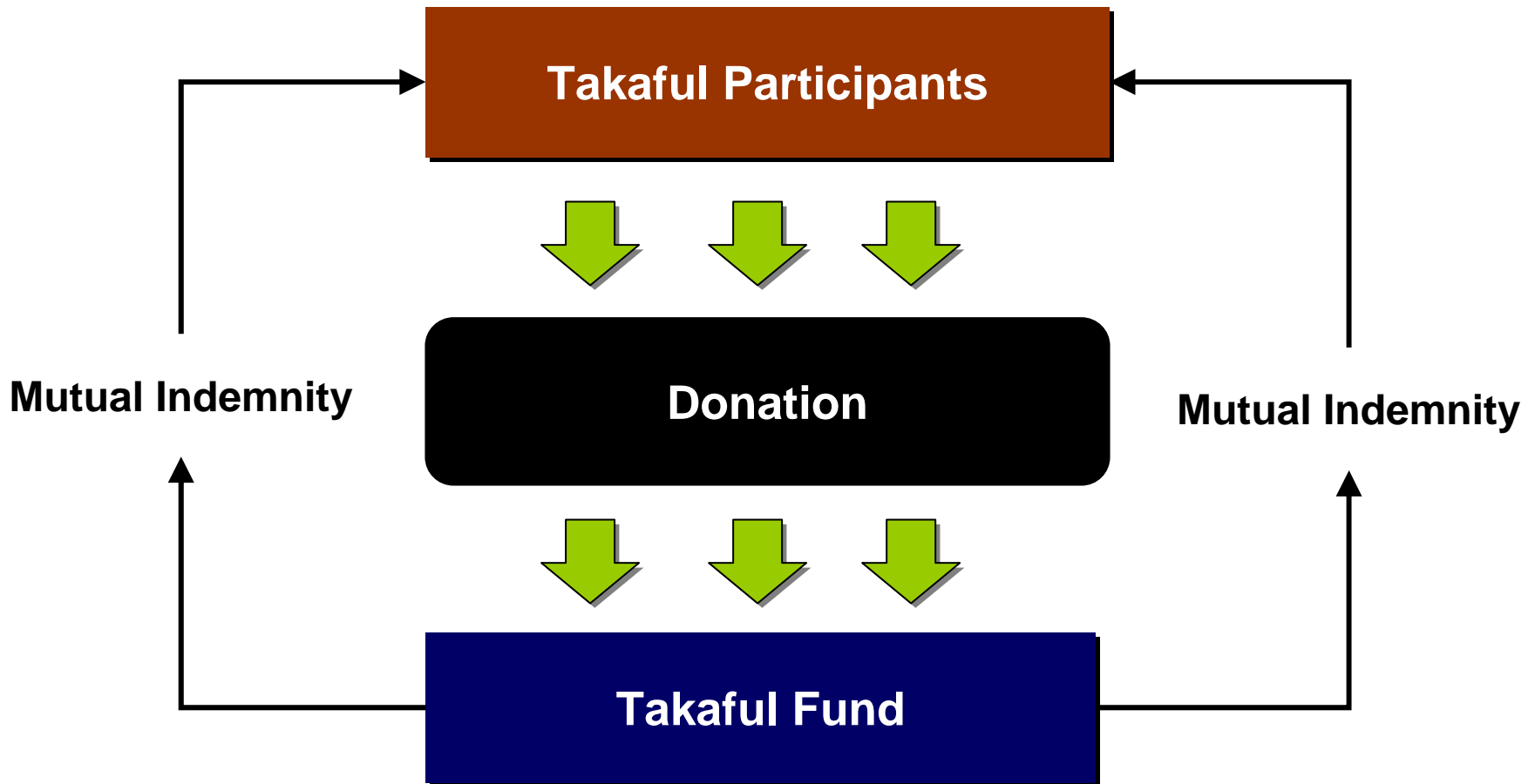
Bank sells on a spot basis the Commodity to Broker B for USD10 million

APPLICATION OF ISLAMIC CONTRACTS IN TAKAFUL

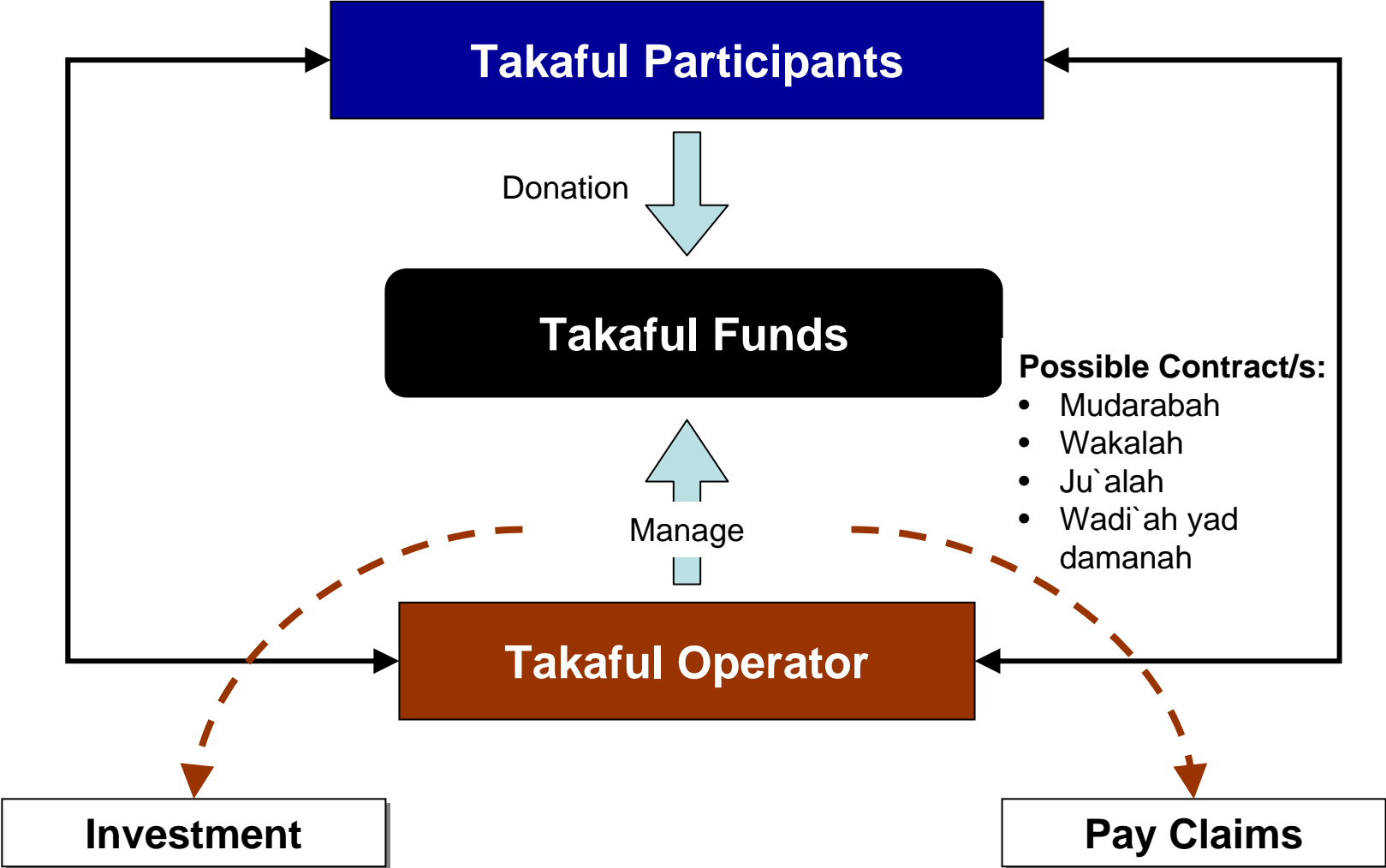
- Contract among Takaful Participants – Tabarru`
- Contract between Takaful Participants & Takaful Operator



CONTRACT AMONG TAKAFUL PARTICIPANTS: TABARRU'



CONTRACT BETWEEN TAKAFUL PARTICIPANTS & TAKAFUL OPERATOR



CONCLUSION



- There is a wide range of contracts that can be applied in structuring & developing Islamic financial services products
- The choice of contracts depends on the purpose and needs of the parties (financial institutions & their clients)
- For example, sales contracts have been widely used for the purpose of financing, especially for asset financing
- Other contracts like leasing and partnership are also widely applied in project financing and securitization transactions
- Takaful industry uses more of donation, agency & investment contracts
- There is always room for more application & diversification of Islamic contracts in Islamic financial services products

THANK YOU

Wassalam

