

Structuring Shariah-Compliant Real Estate Funds

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Topics

- Requirements of Islamic investors regarding real estate investments
- Constraints for investments and financing of the Fund
- Shariah board observance and investors' rights
- Eligible Fund structures for Islamic real estate funds

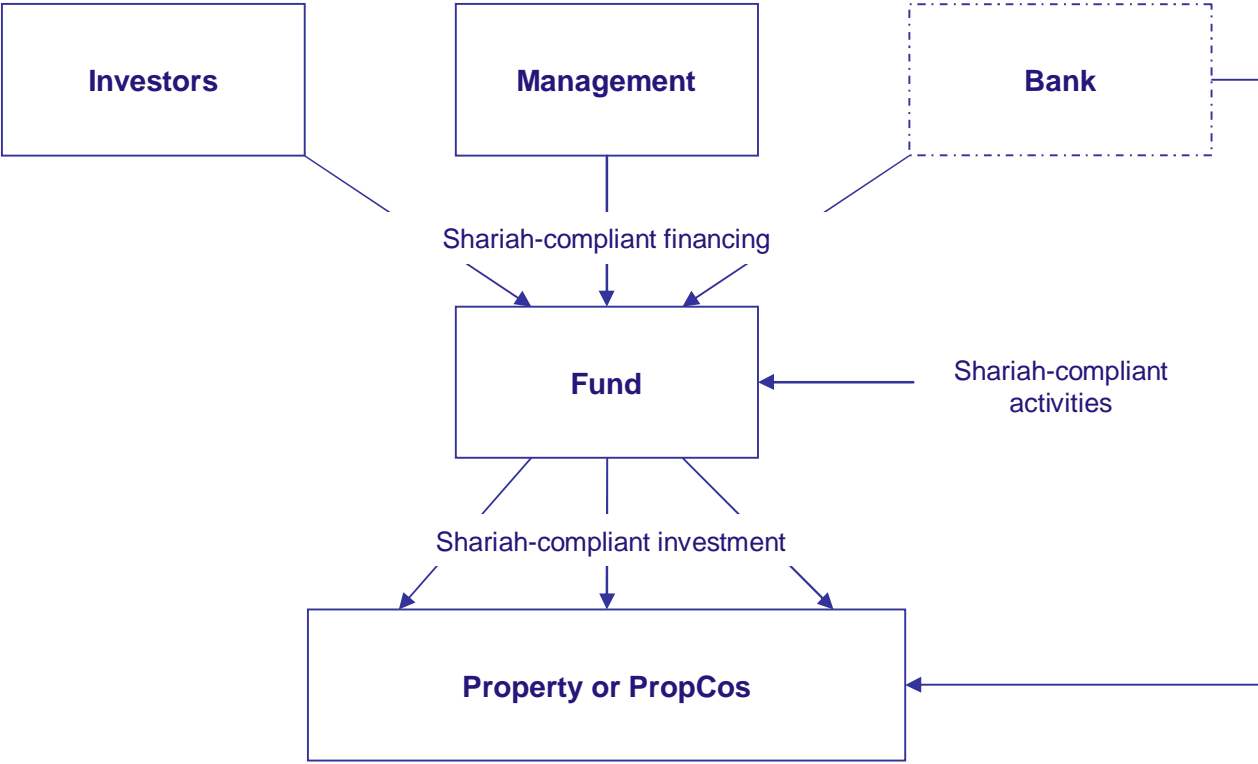
Introduction

- Real estate is preferred asset class for Islamic investors
 - Tangibility of asset class
 - Traditional way of increasing personal value
 - No Zakat (charity tax) payable on value of real estate
- Asset class with broad consistency of the four main Islamic schools regarding interpretation of Shariah; facilitates structuring and marketing of real estate investments
- Steady cash flow for investors

Requirements of Islamic Investors regarding Real Estate Investments

- Investments and investment structures must comply with the principles of Shariah (e.g. profit and risk sharing, ban of rîba and gharar, no prohibited industries)
- Shariah-compliant leverage of investments
- Supervision of fund investments by renowned Shariah board
- Returns comparable to conventional real estate funds
- Tax beneficial fund structures
- Islamic window at conventional real estate funds

Complying with the Islamic Triangle



Investment Constraints

- Fund purpose and investment policy must be Shariah-compliant
- Application of principles to each tenant and each tenant's lease
- Strict interpretation of Shariah or "core business approach"
- Prohibited activities limit eligible tenants and real estate investments
- Phase-out provisions
- è Limitation of discretionary sourcing of investments by fund management
- è Shariah-compliant investment policy as part of fund documentation (LPA, Rulings of Shariah board, PPM)

Financing of Fund and Investments

- Equity financing on fund level is Shariah-compliant
- No fixed or guaranteed profit or return on investment for investors
- No interest payments and no interest income by the fund
- No conventional leverage of fund investments
- Complying with halal financial parameters (see Dow Jones Islamic Finance Index Standards)
- Using Shariah-compliant acquisition financing structures (e.g. Murabaha, Ijara-lease, Musharaka)

Management of Fund Assets

- Shariah looks through the fund
- Sourcing of eligible investments and consulting with Shariah board
- Permanent observance of investments regarding Shariah compliance
 - Negotiation of amendments to lease agreements
 - Screening of new tenants in case of change of tenants
 - Shariah-compliant refinancing of PropCos
- Using Shariah-compliant structures for deposit of liquid funds (Tawarruq-structures)

Shariah Board Observance and Investors' Rights

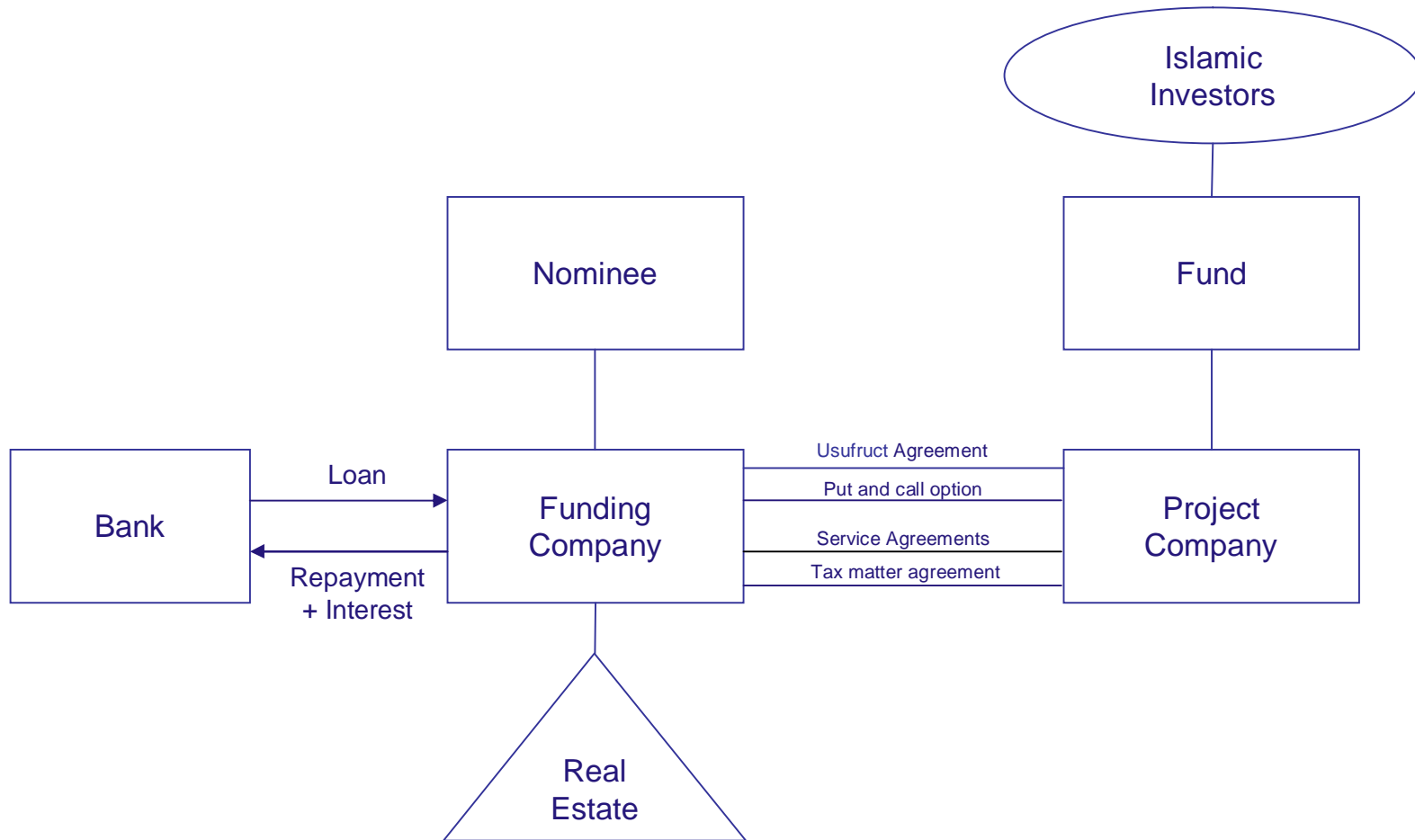
- Implementation of Shariah board is must have
- Composition of Shariah board
- Function and rights of Shariah board
- Opt-out clauses for investors in case of non-Shariah-compliant investments
- Purification of income

Eligible Fund Structures for Islamic Real Estate Funds

- Definition of Funds pursuant to AAOIFI (Accounting and Auditing Organisation for Islamic Financial Institutions):

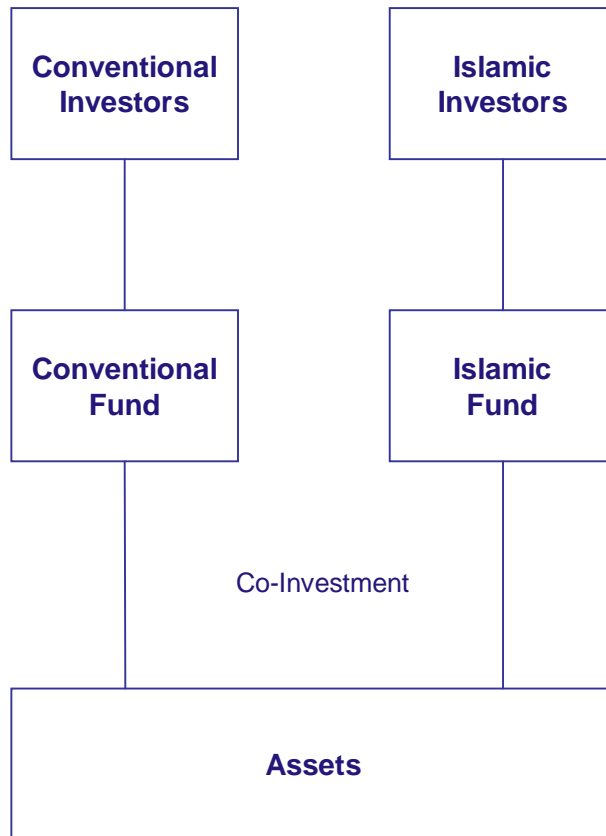
"Funds are investment vehicles, which are financially independent from the institutions that establish them. Funds take the form of equal participating shares / units, which represent the shareholders' / unit holders' share of the assets, and entitlements to profits or losses. The funds are managed on the basis of mudaraba contract."
- Islamic Fund structures based on mudaraba (or musharaka) contracts
- Mudaraba structure:
 - Investor = rabb al-mal
 - Manager = mudarib
- Conventional fund structures like limited partnerships mostly comply with Islamic Fund Structure approach
- Management / performance fees for management are Shariah-compliant

Example of Real Estate Fund Structure using Ijara-Lease Structure

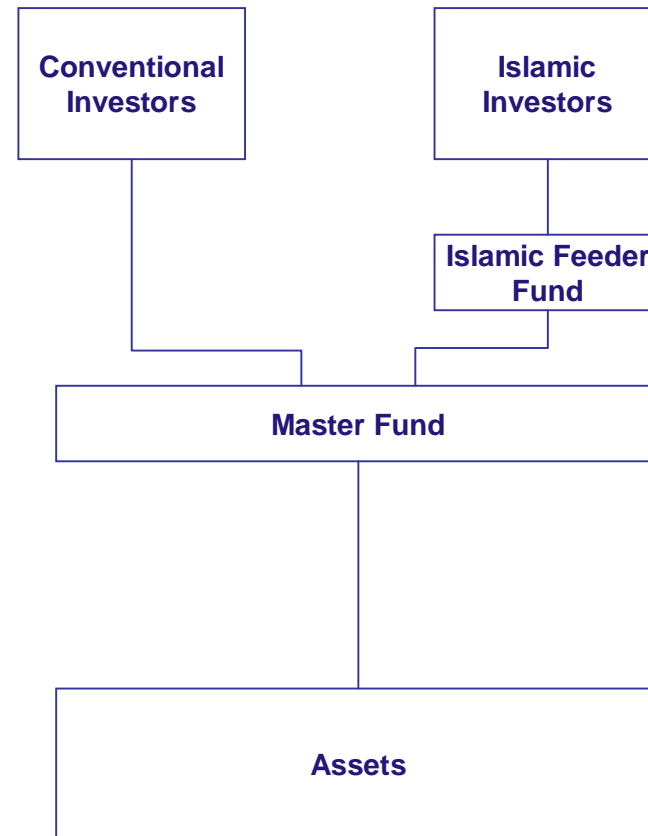


Fund Structures for Conventional and Islamic Investors

Parallel Fund Structure



Master-Feeder-Structure



Q & A

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