

A Takaful Wrapper for Sukuk Issues

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Rabel Akhund

Islamic Finance Group

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Takaful: Background and some opportunities

- Conventional insurance problematic under Shariah.
- Problems with Gharar, riba and gambling.
- Takaful based on pooling of risks and concepts of mutuality.

Historical Background - Sukuks

- Need for liquidity and good liquidity management
- Different periods between maturities of assets and deposits – resulting in either surplus of non performing cash or a shortage of cash to fund investments
- Lack of:
 - active interbank and secondary market (mostly primary market trading)
 - acceptable Shariah compliant instruments
 - acceptable regulatory conditions
 - limited available agency credit ratings
 - unsophisticated market
 - limited information flow

Coming together of the various Islamic Finance products into a more sophisticated capital, financial and insurance market.

Sukuks – Legal Meaning

- All this changed with the development of the Sukuks.
- Definitions:
 - a) “Participation Securities, coupons, investment certificates”
 - b) “Certificates of equal value, representing after closing subscription, receipt of the value of the certificates and the putting to use as planned, common titles to shares and rights in tangible assets, usufructs and services, or equity of a given project or equity of a special investment activity”

Types of Sukuks

- MUDARABA SUKUK
- SALAM SUKUK
- IJARA SUKUK
- DEVELOPMENT SUKUK (ISTISNA)
- MUSHRAKA SUKUK

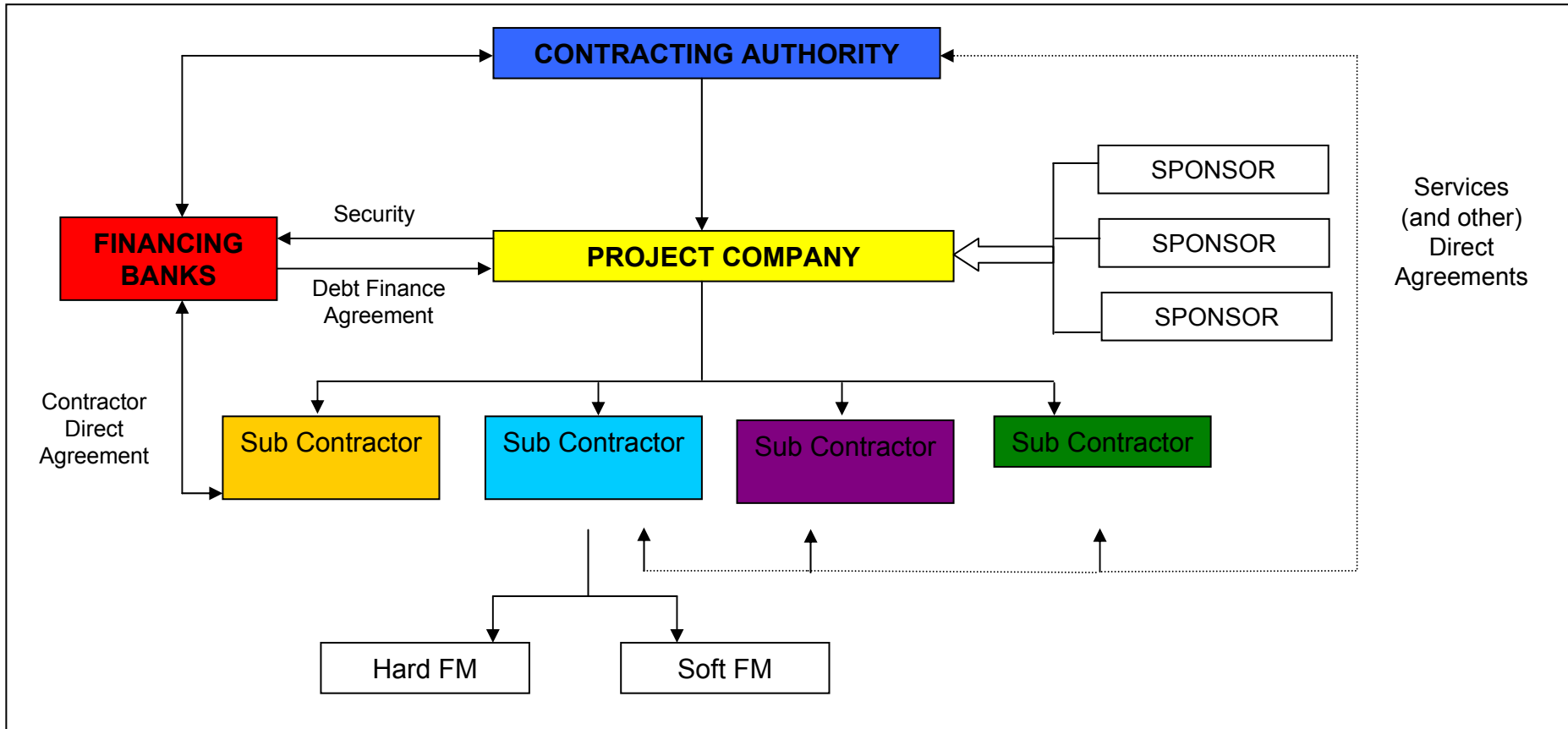
Types of Sukuks

- Other Derivations/hybrids
 - Pure Ijara
 - Pooled/hybrid SUKUK (underlying assets use a variety of structures)
 - Variable rate SUKUK
 - Zero-coupon SUKUK

Ijara (Leasing) Sukuk

- can be used for long term infrastructure projects by the mobilisation of short term deposits i.e. securitisation of Government tangible assets
- possible use in project financings.

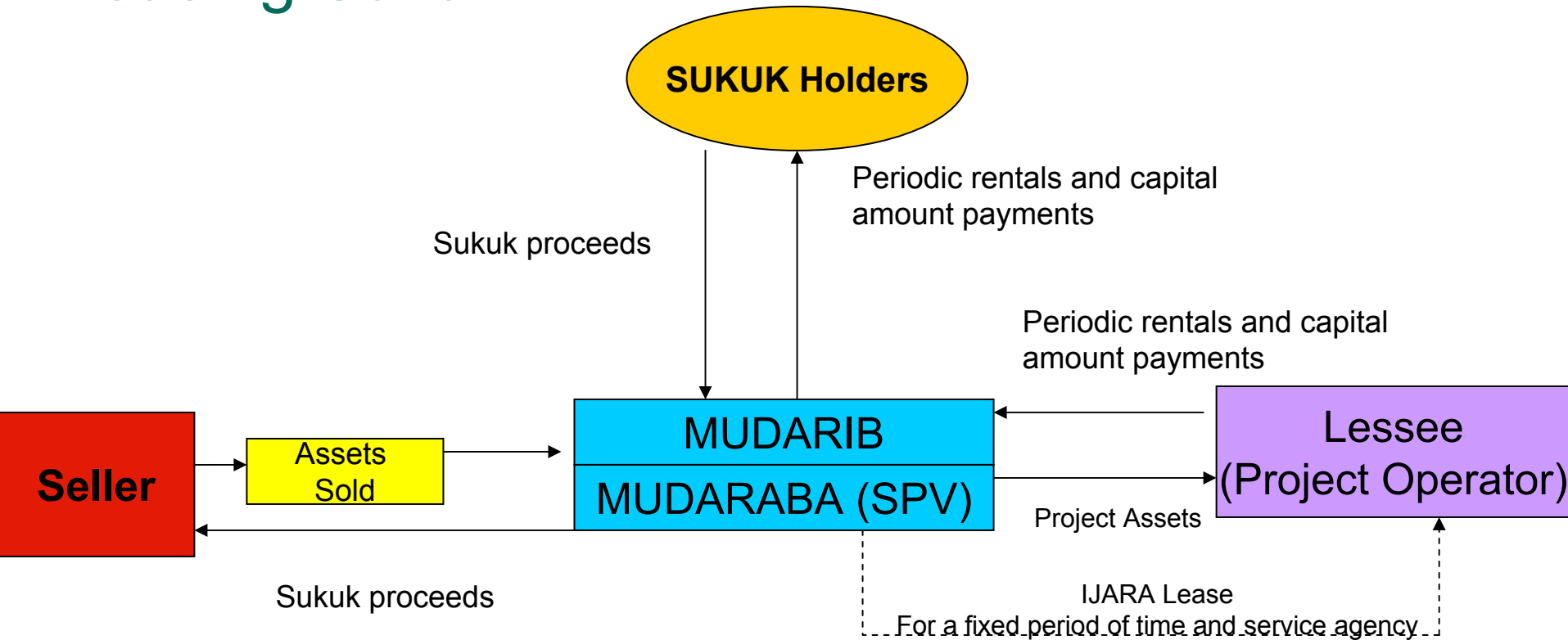
Typical Project Financing Structure



Ijara (Leasing) Sukuk

- Works as follows:-
 - sale of tangible assets to a special purpose restricted Mudaraba (SPV)
 - assets are then leased to the interested parties through a Ijara lease
 - the MUDARABA participation SUKUK will be issued and sold to public/investors with a guarantee of payments (usually from Government or international bank)
 - required security will be given to SUKUK holders
 - MUDARABA managed (on behalf of SUKUK holders) by MUDARIB
 - MUDARIB signs and executes all relevant contracts
 - ensures Shariah compliance
 - transparency and efficient operation

Leasing Sukuk



Conventional Monoline Wraps

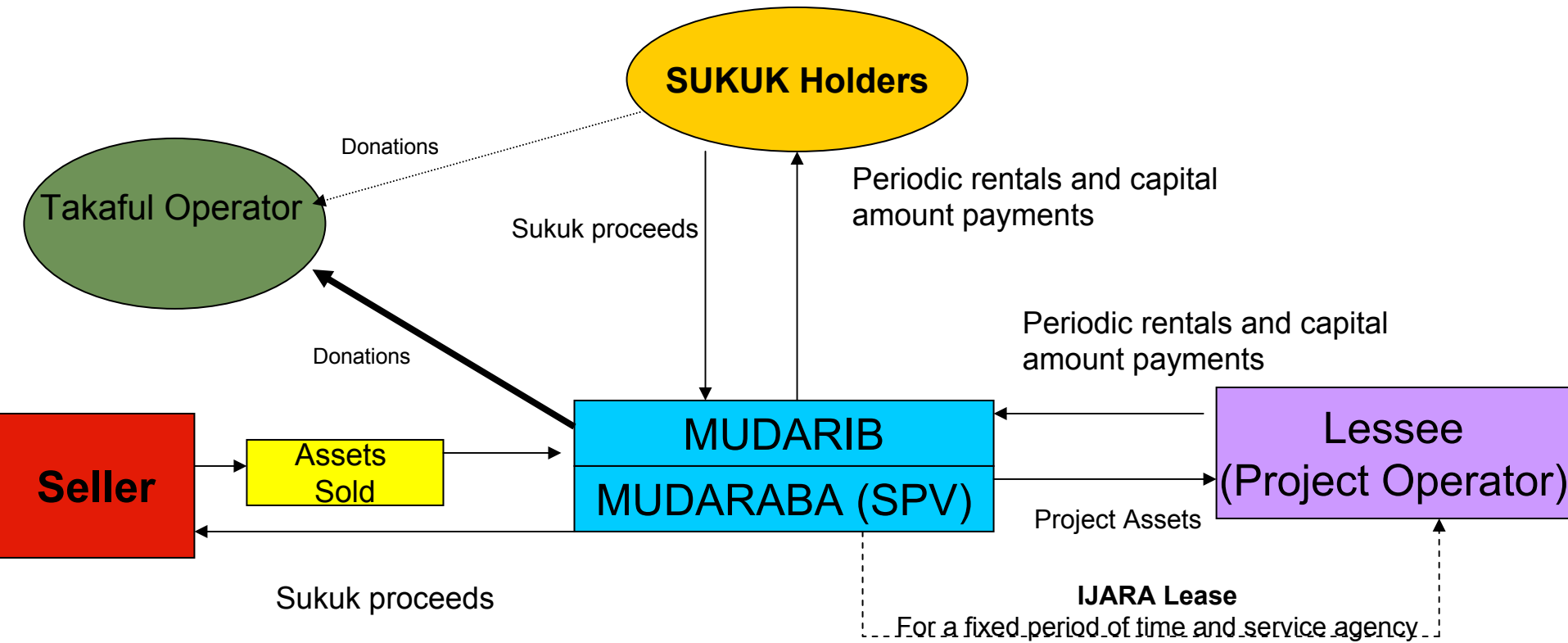
- **Coventional Monoline Insurers**
 - **Credit Enhancement**
 - **MBIA, FSA and FGIC**
 - **Guaranteed timely payments of Interest and Principle**
 - **Similar problems faced by conventional insurance under Shariah.**
 - **Security**
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- **A Matter for Discussion: Pushing the Takaful industry into new areas including trading surpluses.**

Takaful Wraps

- **The Need to Challenge the Market**
- **Go beyond the traditional usage of Takaful**
- **Structures that could work are as follows:**
 - a) **Wakala (Agency)**
 - b) **Mudaraba (more effective)**

Mudaraba

- **Options available**
 - a) **Mudaraba with Sukuk Holders on the basis of a portion of the subscription monies designated as donations.**
 - b) **Mudaraba with Issuer of Sukuks on the basis of a donation paid by the Issuer from the subscription proceeds of the Sukuks (more effective).**
- Grant of security from Issuer more appropriate.**



Takaful and Sukuks

- **One helps the other.**
- **Concept of a surplus float.**
- **Sukuks have created increased liquidity in the traditional Islamic capital markets.**
- **That means that Takaful companies can invest the surplus float in Sukuks, giving them more Shariah compliant avenues for investment of the float.**

RABEL AKHUND
Taylor Wessing
Carmelite
50 Victoria Embankment
Blackfriars
London
EC4Y 0DX

Tel: 0207 300 7000

Fax: 0207 300 7100

Direct Dial: 0207 300 7096

E-mail: r.akhund@taylorwessing.com

Web: www.taylorwessing.com