

Session 1

Shari'ah Risk in Product Development, Processes and Operations

Islamic Equity Indices and their use in Islamic Fund Management

Rushdi Siddiqui, Global Head of Islamic Finance, Thomson Reuters









Presentation Overview

- **Thomson Reuters**
- **Islamic Equity Funds**
- **Whats at Stake? Systemic Confidence**
- **Shariah Screening Risks**
- **Shariah Fund Management Risks**
- **Governance: Islamic Information Gateway Platform**
 - ▶ Islamic Indexes
 - ▶ Islamic Funds Supermarket

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Shari'ah Risk In Equity Screening

What's at Stake? Systemic Confidence

■ 561 Islamic Funds (Q2, '09)*

▶ 304 Islamic Equity Funds	(55%)
▶ 98 Mixed Funds	(17%)
▶ 72 Money Market Funds	(13%)
▶ 59 Bonds Funds	(11%)
▶ 14 Real Estate Funds	(3%)
▶ 14 Other	(3%)

■ Total AUMs **\$25B (12/2008)**

■ *Lipper

Shari'ah Risk in Equity Screening

■ Index Providers

- ▶ DJIM
- ▶ FTSE Shariah
- ▶ MSCI/Barra Islamic Indexes
- ▶ S&P Shariah Indexes
- ▶ Russell

■ Financial Institutions

- ▶ GIH, Shuaa, HSBC, etc.

■ Regulators

- ▶ SC (Malaysia)

■ Stock Exchange

- ▶ DFM (Dubai)

■ Standard Setting Body

- ▶ AAOFI (Bahrain)

Shari'ah Risk (SR) In Equity Screening

- **SR on Islamic Index Construction**
 - ▶ Creation
 - Negative screening → Positive Screens (Sustainability)
 - Mechanical v. Subjective
 - ▶ Continued Compliance

- **Primary Business**
 - ▶ Division & Subsidiaries & Corresponding Revenue Accountability
 - Islamic Banks/Takafol/Mortgage?

- **Financial Ratios**
 - ▶ Leverage/Gearing Screen
 - Islamic Debt (Malaysia v. GCC)

- **Reviews**
 - ▶ Real-Time, Monthly, Quarterly or Semi-Annually

- **Purified Islamic Indexes**

- **Probation**

Shari'ah Risk (SR) In Islamic Equity Funds

- **Shari'ah Board/Advisors?**
- **Licensee of Index Provider**
 - ▶ Going Outside the Benchmark
 - ▶ Company Deletion from Islamic Index?
 - Probation
 - ▶ Shadow Indexing → Non-compliant company?
- **Parking Cash & Redemptions**
 - ▶ Non-Muslim country based Islamic funds
- **Leverage & Derivatives**
- **Purification Calculation**
- **Zakat Calculation**

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- Precedent Disclosures

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- Basis Point
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- Applied Islamic Law of Trade and Finance
- Applied Takaful and Modern Insurance: Law and Practice
- Law and Practice of Islamic Banking and Finance

International Financing Review

- International Financing Review
- IFR Intelligence Reports
- IFR Roundtables

STANDARDS, RULINGS & LAWS

Standards

- Islamic Financial Services Board (IFSB)
 - Published Standards
 - Exposure Drafts
 - Other Documentation
- UK Law
 - UK Case Law
 - UK Acts
 - FSA Handbook (Rules)

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1. ATLANTIC FINANCE LTD

Issue Date: 21 May 2009 Domicile: Jersey

...Chairman of The National Central Cooling Company PJSC, the Chairman of Aabar Investments PJSC, the Chairman of Abu Dhabi National Takaful Co and the Vice Chairman of Abu Dhabi Polymers Co. Ltd (Borouge). He is also a board member of Borealis AG

Annual Reports

Show Annual Reports

1. AL ZAMIN LEASING MODARABA

Date: 7 October 2008 Domicile: Pakistan

...2008 Note 2008 2007 Assets Current Assets Cash and bank balances 5 186,803,085 212,594,086 Short term investments 6 50,750,105 53,926,953 Takaful Reserve Fund Investments 7 44,727,900 47,298,558 Short term musharakah and murabahah 8 538,625,830 417,361,955 Advances and prepayments 9 44,328,221 36 ...39,998,660 6.3 Available for sale Number of ordinary shares Market value 2008 2007 2008 2007 100.000 Dawood Family Takaful Limited 6.3.1 1.000.000 100,000 Rupees 1,000,000 6.3.1 1 he above company currently is not listed. 7. TAKAFUL RESERVE FUND INVESTMENTS 2008 2007 Available for sale At fair value through profit or loss upon initial 71 44,727,900 recognition ...up to a maximum of 10% of the equity of the Modaraba shall always be kept separately and embarked against Takaful reserve Fund. At 30 June 2008, the Modaraba's Takaful Reserve Fund investment was 11.52% of its Modaraba. Accordingly arrangements are being made to address the above restriction. 7

FSA Listings

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1. UKOFFERING

Company: ABU DHABI COMMERCIAL BANK P J S C File Number: Filed: 07/07/2009

Full Text Offerings

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8/7/09 New Straits Times (Pg Unavail Online)
2009 **WJHR** 1529483

New Straits Times
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August 7, 2009

Petronas to tap South China Sea oil, gas fields?

MALAYSIA has proposed that Brunei consider the possibility of Petronas playing a role in the disputed territories in the South China Sea, which are known to have large deposits of oil and gas. Prime Minister Datuk Seri Najib Razak said the role by Petronas could be worked out within the framework of what has been agreed upon in the Exchange of Letters signed by both countries early this year. "I don't want to go into specifics, but the Brunei side is aware of some of the things that we would like to see take into account." Asked whether the proposal would involve joint exploration of oil and gas in the disputed areas by Malaysia and Brunei, Najib said the matter would be discussed later.

He was speaking at a news conference at the end of his three-day official visit here for the 13th Annual Leaders' Consultation between Malaysia and Brunei. Najib arrived here on Tuesday accompanied by his wife Datuk Seri Rosmah Mansor, eight ministers and the chief ministers of Sabah and Sarawak. The dispute arose in 2003 when Brunei and Malaysia awarded petroleum production blocks in the South China Sea, close to what a discovery block in the area. The blocks are worth an estimated \$44 billion. Brunei reportedly awarded one of its exploratory blocks to France's Total, BHP Billiton and Hess Corp and the other to Shell, Mitsubishi and ConocoPhillips, while Malaysia's Petronas awarded its two blocks to US firm Murphy Oil. The overlapping territorial claims by both countries also involved Limbang, a small town north of Sarawak. Located on the banks of Sungai Limbang between the two halves of Brunei and covering an area of 3,978 sq km, Limbang was annexed by Charles Brooke, the second Rajah of Sarawak, in 1890 to become the fifth division of Sarawak. Malaysia and Brunei signed on March 16 an Exchange of Letters towards a milestone settlement of the disputed territories. The letters contain several principles of cooperation to be implemented in the surveying and demarcation of the land and maritime borders. Following the signing of the Exchange of Letters, a joint Brunei-Malaysia technical committee was set up to transfer to the ground the territorial dispute settlement. The responsibility of the committee is to settle technical issues related to surveying, delimiting and demarcating both land and maritime boundaries between the two countries. Najib said he believed that with the existing close and friendly ties between Malaysia and Brunei, both countries would be able to resolve the land and maritime border demarcation without any problem. Explaining that the survey and demarcation work would take time to complete, the prime minister said there was no specific time-frame for the matter to be finalised. "There is still quite a large stretch that needs to be surveyed and demarcated on the ground and it might take a bit of time." The important thing is that there is a principle agreement on both maritime and land, so we can now move forward and not allow to be in the way of improving bilateral ties." The prime minister said Sultan Hassanah Bolkiah had, in his meeting, expressed satisfaction over the progress made in realising the objectives of the Exchange of Letters. "The Sultan is also satisfied with the level of bilateral relations between both countries and hopes it could be enhanced further," Najib said, noting that several successful collaborations have been discussed. Najib hoped that the numerous proposed collaborations would yield results before the next Annual Leaders' Consultation in Malaysia next year. He said the eight ministers who accompanied him had been tasked to discuss with Brunei counterparts the prime minister's proposal on expanding the area of collaboration, including in the surveying and demarcation of the land and maritime borders. He also welcomed in the Sabah Development Corridor, Sarawak Corridor of Renewable Energy and Iskandar Malaysia in Johor. (END)

--- INDEX REFERENCES ---

COMPANY: RENEWABLE ENERGY HOLDINGS PLC, CONOCO-PHILLIPS CO, SABAH, RENEWABLE ENERGY GENERATION LTD, BHP BILLITON LTD, HESS CORP, BHP BILLITON PLC

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GSII IFBF 2.3
Analytical Materials - 2.3: Islamic financial products in Malaysia

Islamic Banking and Finance 2.3

Law and Practice of Islamic Banking and Finance Database updated April 2009

Dr Nik Norzuli Thank, Mohamed Ridza Mohamed Abdullah, Megat Hisham Hassan

Chapter 2: Islamic Financial Products: History and Concept

2.3. Islamic financial products in Malaysia

Islamic banking is starting to flourish in Malaysia, especially in the country's aim towards achieving positive growth. When domestic capital is found to be inadequate to provide for such growth, the economic planners have come with 2 major options viz to internally savings and to attract foreign equities. Efforts to attract foreign portfolio investment into Malaysia is not as easy as it is thought. To depend on foreign savings will also imply the ability to handle problems that may arise. Today, efforts have been made to attract portfolio capital from the Middle-East to complement the much needed capital inflows that Malaysia needs. It is assumed that there are several factors which play an important role in determining capital flows from the Middle eastern countries, such as the nature of the activities carried out, the prospect of currency fluctuation and also the uncertainties in the financial market as well as less predictable monetary and fiscal policies introduced by the Malaysian Government. Apart from that, another vital factor is the acceptance of financial products used by the Middle East investor.

Since the launching of Malaysia's first Islamic bonds as early as 1992, a total of RM20.5 billion has been invested in Islamic bonds since then. However, there are critics directed to the nature and system of administration and management of the bonds itself especially from the Middle-Eastern investors, individual Islamic jurists and thinkers in the Middle East who have raised concerns about the structure and the techniques used for the securities issues and concepts, such as *Bar'Al-Dayn* and *Bar'Al-Ijarah*, which have been used to a large extent and have raised dispute over the acceptability of such concepts under Islamic financial principles. The author has had experiences dealing with parties and scholars in the Middle East and also countries in South East Asia wherein these individuals are hesitant to embrace the Islamic financial methodology which is practiced in Malaysia. Following from that, it is a challenge for the Islamic scholars in Malaysia to be able to come up with Islamic products which are not just acceptable in Malaysia but also in the Muslim world at large. For the remaining part of this chapter, the author will explore the various Islamic financial products which are acceptable and have been utilized by the financial community in Malaysia. In exploring the various Islamic financial products available, references to the Accounting and Auditing Organisation for Islamic Financial Institutions will also be made for some of the products in deriving the permissibility of some rulings under the *Shariah*.

Al-Bai' Bithaman Ajil (Credit Sale)

The most popular Islamic banking transaction seems to be Al-Bai' Bithaman Ajil. This is an agreement whereby a bank buys an asset or property and sells the said asset or property to a customer at an agreed deferred price when the customer has to pay on a deferred basis or by periodic instalments. (See *The Ahsanul Fiqh: Contracts of Exchange in Al-Quran: An Introduction to Islamic Finance*, by Haid Ibrahim Halim at pp 298-301). At a quick glance, this is no different from a common sale and purchase agreement where the vendor permits the purchaser to pay the sale price by instalments provided it satisfies all relevant *Shariah* elements. It is an agreement that refers to the sale and purchase transaction for the financing of an asset on a deferred payment basis with a pre-agreed payment period. The sale will include a profit margin.

Under this principle, the borrower is allowed to postpone the settlement of payments for goods bought within a certain period of time agreed and enhanced upon, and also in accordance with the methods determined and agreed upon by both parties. (See *Islamic Banking: Its legal environment* by legal reference to Malaysia, Law Majalla (2002), an article by Zamri bin Ali Hassan).

The suitability of credit sale is found in the *Sunnah* in which the Prophet was reported to have said:

Three things none which have a blessing in it, namely, credit sale, *Muqadadnah* (*Mudharabah*), and a mixture of four and barley for the purpose of irrigation, and for the purpose of sale.

One does not need to have a legal interest or be a registered proprietor of the property or have full beneficial interests to be able to sell the property in an Al-Bai' Bithaman Ajil transaction. By the customer executing the sale and purchase agreement with the vendor, it would entitle the customer to 'sell' such rights to the financing bank for the loan.

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IFSB 6 - Guiding Principles on Governance for Islamic Collective Investment Schemes

Original Document in Arabic

Original Document in English

Image 1 in PDF format Not available for Offline Print

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ISLAMIC FINANCIAL SERVICES BOARD

GUIDING PRINCIPLES ON GOVERNANCE FOR ISLAMIC COLLECTIVE INVESTMENT SCHEMES

January 2009

ABOUT THE ISLAMIC FINANCIAL SERVICES BOARD (IFSB)

The IFSB is an international standard setting organization that promotes and enhances the soundness and stability of the Islamic financial services industry by issuing global prudential standards and guiding principles for the industry, broadly defined to include banking, capital markets and insurance sectors. The standards prepared by the IFSB follow a lengthy due process as outlined in the Guidelines and Procedures for the Preparation of Standards/Guidelines, which includes the issuance of exposure drafts and the holding of workshops and, where necessary, public hearings. Research and coordinate activities on industry-related issues as well as organise roundtables, seminars and conferences for regulators and industry stakeholders. Towards this end, the IFSB works closely with relevant international, regional and national organizations, research/educational institutions and market players.

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 - IFSB 7 - Capital Adequacy Requirements for Sukuk Securitisations and Real Estate Investment
 - Guidance Note in Connection with the Capital Adequacy Standard: Recognition of Ratings by External ...
 - Exposure Drafts
 - Exposure Draft 8 - Guiding Principles on Governance for Islamic Insurance (Takaful) Operations
 - Exposure Draft 9 - Conduct Of Business For Institutions Offering Islamic Financial Services (IFS)
 - Exposure Draft 10 - Guiding Principles On Shari'ah Governance System
 - Other Documentation
 - Technical Note on Issues in Strengthening Liquidity Management of Institutions Offering ... (March 2008)
 - Compilation Guide on Prudential and Structural Islamic Finance Indicators: Guidance ... (November 2007)
 - Islamic Financial Services Industry Development: Ten-Year Framework and Strategies (May 2007)
 - Issues in Regulation and Supervision of Takaful (Islamic Insurance) by IFSB and International ... (August 2006)
 - IFSB Guidelines and Procedures for the Preparation of Standards/Guidelines

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