



UPPSALA  
UNIVERSITET

Uppsala Faculty of Law  
Working Paper 2017:2

# An Introduction to Islamic Securities (Sukuk)

Pegah Zolfaghari



## **Abstract**

Islamic securities (Sukuk) are hybrid securities bearing features of stocks and bonds, altogether. Similar to stocks, they indicate a type of partnership and holders of Sukuk will be considered as the owners of underlying asset or project for finance of which, Sukuk have been issued. Theoretically, these holders share any loss and profit resulted from underlying asset. However, these securities usually bear a maturity date like bonds and contrary to stocks. The holder has no voting right or control over the underlying asset. In case of bankruptcy and contrary to the shareholders, holder benefits from priority right over underlying asset, in comparison to other creditors. Practically and contrary to the initial theory in consideration of Sukuk (sharing in loss and profit), nowadays some of these securities are usually of fixed revenue and any probable risk resulting from decrease being made in the value of underlying asset will be covered by the issuer or originator, through insurance companies. Nowadays, new forms of Sukuk such as convertible, preference, subordinated and perpetual Sukuk have been developed, features of which are very similar to hybrids. Considering special nature of Sukuk, indicating partial ownership of its holder over related underlying asset or project, somehow we may use these new hybrid tools to prevent prevailing risks related to other securities and hybrids, such as credit and bankruptcy risks; and, we may use them more in financing and attracting capital, globally.

Working paper 2017:2

An Introduction to Islamic Securities (Sukuk)

Pegah Zolfaghari

PhD student in private law, Shahid Beheshti University of Iran

Visiting researcher at Uppsala University in 2017

[p\\_zolfaghari@sbu.ac.ir](mailto:p_zolfaghari@sbu.ac.ir)

Tillgänglig via <http://uu.diva-portal.org>

## Contents

|          |  |           |
|----------|--|-----------|
| <b>1</b> | <b>Introduction</b>  | <b>4</b>  |
| <b>2</b> | <b>What is Sukuk?</b>  | <b>5</b>  |
| 2.1      | Definition of Sukuk  | 5         |
| 2.2      | Benefits of Sukuk  | 6         |
| 2.3      | Main players in the Sukuk market   | 6         |
| 2.4      | Sukuk; Equity or Bonds?  | 7         |
| 2.5      | Asset backed-Sukuk   | 8         |
| 2.6      | Asset-based Sukuk  | 8         |
| 2.7      | Comparing Asset-based and Asset-backed Sukuk with other Forms of Securities  | 12        |
| 2.8      | Differentiation Aspects of Sukuk and Bonds   | 15        |
| 2.8.1    | Concept of Converting Assets to Securities (securitization) in Terms of Sukuk  | 17        |
| 2.8.2    | Concept of Asset in Terms of Sukuk   | 19        |
| 2.8.3    | Concept of SPV (special purpose vehicle) in Sukuk: The Difference between SPV as an Intermediary in the Process of Issuance of Sukuk and the Concept of Intermediary in Conventional Bonds | 19        |
| 2.8.4    | Difference of Sukuk and Common Bonds, in Case of Bankruptcy of the Intermediary  | 20        |
| 2.8.5    | Comparing Concept of Ownership in terms of Sukuk and Indirect Holding in Conventional Bonds  | 22        |
| 2.8.6    | Comparing Registered and Non-Registered Sukuk with Other Securities in This Respect  | 24        |
| 2.8.7    | Sukuk-Related Challenges in Comparison to Conventional Bonds   | 25        |
| <b>3</b> | <b>Sukuk Is a New Type of Hybrid Securities</b>  | <b>27</b> |
| 3.1      | What is a Hybrid Security?   | 27        |
| 3.2      | Sukuk and Hybrids  | 27        |
| 3.3      | Different Types of Hybrids and Comparison to Sukuk   | 30        |
| 3.3.1    | Convertible/Converting Debt Security and Sukuk   | 30        |
| 3.3.2    | Preference Shares and Sukuk  | 31        |
| 3.3.3    | Capital Notes  | 32        |
| 3.3.3.1  | Perpetual debt securities and Sukuk  | 32        |
| 3.3.3.2  | Subordinated debt securities and Sukuk   | 33        |

*An Introduction to Islamic Securities (Sukuk)*

|          |  |           |
|----------|--|-----------|
| 3.3.3.3  | Knock-out debt securities and Sukuk                    | 33        |
| 3.3.3.4  | Risks of Conventional Hybrids in Comparison with Sukuk | 34        |
| <b>4</b> | <b>Conclusion</b>                                      | <b>35</b> |
|          | <b>Appendix</b>  | <b>37</b> |
|          | <b>References</b>                                      | <b>38</b> |

# 1 Introduction

Sukuk (Islamic securities) are considered as Islamic financial instruments created for middle and long term financing due to some limitations existing in Islamic financial system, resulting in lack of use of common bonds. These instruments are very similar to common bonds; however, there are some differences also between the two and in some cases they bear characteristics of stocks. This has resulted in Sukuk (Islamic securities) to be (probably) considered as a type of hybrid financial instrument. Outside Islamic financial system, hybrid instruments are considered as one of the prevailing and common types of securities. These instruments are divided into several categories, each of which having characteristics of both bonds and stocks. Considering the point that Sukuk are not specifically used in Islamic markets and they are also applicable in other capital markets as a financing tool, in this paper, Sukuk will be introduced and compared with prevailing securities in non-Islamic systems. It will also be discussed whether Sukuk might be of use as a hybrid security in non-Muslim majority capital markets, just the same as other common hybrids because Sukuk are of such a structure which might be free from risks available in terms of other types of hybrids; while, they are similar in their advantages. This paper aims to introduce and examine Sukuk in comparison with other securities of various aspects so that the concept and nature of Sukuk would be more tangible and easier to understand for the reader. In the other words in this paper we declare the differences or similarities between Sukuk and other securities in terms of the bankruptcy of intermediary, the concept of intermediary, the concept of asset and securitization and also other concepts. At the end, we want to compare Sukuk and hybrids and express instances of Sukuk which are similar to hybrids so that we make understanding of Sukuk as a hybrid, more tangible. For this purpose, in the first part of the paper we introduce Sukuk, benefits of that and main players in Sukuk market. In second part, we compare Sukuk with bonds and shares in different aspects, for this reason we will introduce two general models of Sukuk that are asset-backed and asset-based Sukuk and compare each of them with other securities and declare that asset-backed Sukuk is more like shares and asset-based Sukuk is more like bonds. While second type of Sukuk does not match to draft standards of Sukuk that we can observe in asset-backed Sukuk, today it has become increasingly popular.

Followed by expression of similarities between asset-based Sukuk and bonds, we express differentiation aspects of Sukuk (here we more mean asset-backed Sukuk) and bonds and deal with their seven fundamental differences. We also express that what similarities and differences there are between Sukuk and conventional bonds on the concepts and issues such as securitization, asset, intermediary and on supposition of bankruptcy of the intermediary and also on the concept of indirect holding. In the same part, we also introduce registered and non-registered Sukuk and Sukuk-related challenges in comparison to conventional bonds. Finally and in the third part of this article, we introduce Sukuk as a hybrid and express examples of Sukuk that are similar to hybrids like as convertible Sukuk, contingent convertible Sukuk (CoCo Sukuk), preference Sukuk, subordinated Sukuk and perpetual Sukuk.

## 2 What is Sukuk?

### 2.1 Definition of Sukuk

Sukuk are financial instruments similar to bonds and also shares that are compliant with Islamic law. Since their inception in 2002, Sukuk markets have experienced dramatic growth rates attracting the attention of investors, analysts and researchers alike.

Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) defines Sukuk as being: “Certificates of equal value representing undivided shares in the ownership of tangible assets, usufructs and services or (in the ownership of) the assets of particular projects or special investment activities.”<sup>1</sup>

There are three requirements for a Sukuk to be considered in compliance with the Sharia law<sup>2</sup>. First, the certificates must represent ownership in tangible assets, usufructs or services from revenue-generating firms. Second, payments to the investor come from after-tax profits and third, the value repaid at maturity date should follow the current market price of the underlying asset and not the original invested amount. Sukuk comes in many different forms, as financiers are not restricted to create

<sup>1</sup> The AAOIFI Shari'ah Standard (17) on investment Sukuk.

<sup>2</sup>Godlewski, C, Turk-Ariss, R, & Weill, L. ,Sukuk vs. conventional bonds: A stock market.

perspective, Journal Of Comparative Economics, 41, 2013, pp. 745-761.

their own variations<sup>3</sup>, However, fundamentally the parties within a Sukuk issuance are the firm (the obligor or originator), the Special Purpose Vehicle (SPV) and the investors that buy the Sukuk. The SPV is a bankruptcy-remote entity, separate from the originator, which issues Sukuk certificate.

## 2.2 Benefits of Sukuk

Among benefits of Sukuk we can refer to these: Sukuk is tradable capital market product providing medium to long-term fixed or variable rates of return. It is assessed and rated by international rating agencies, which investors use as a guideline to assess risk/return parameters of a Sukuk issue. It has regular periodic income streams during the investment period with easy and efficient settlement and a possibility of capital appreciation of the Sukuk. Finally, Sukuk are liquid instruments and tradable in secondary market.

## 2.3 Main players in the Sukuk market

The Persian Gulf Corporation (GCC) Countries and South East Asia (SEA) countries are the main players in the global Sukuk market. Among the GCC countries UAE, Saudi Arabia, Bahrain, Qatar, Kuwait are important countries in issuing Sukuk. Meanwhile the Malaysia is playing a main role in the region of SEA, other than Malaysia, Indonesia, Singapore also is contributing to the global Sukuk market from this region. Today it is not limited to this region only. It's developing in other countries as well, Pakistan, Japan from other part of Asia other than Asian countries, USA, UK, Germany, Turkey, Egypt, Gambia also are contributing to the market. According to International Islamic Financial Market (IIFM) report in 2016, a positive development in Sukuk market is the appeal of Sukuk as an alternative source of financing from new jurisdictions ranging from Europe, Asia, CIS and Africa and emerging sign of possible direct entry from North America.<sup>4</sup> It should be noted that, in 2000, total size of the Sukuk was only US\$ 1'172 million with no sover-

<sup>3</sup> Visser, H., *Islamic Finance: Principles and Practice*, Gloucester: Edward Elgar Publishing, 2009.

<sup>4</sup> IIFM Sukuk Report (5th Edition) A Comprehensive study of the Global Sukuk Market.

oreign Sukuk in the market. According to IIFM report, in the next 16 years, the total size of Sukuk has crossed US\$ 68'742 million.<sup>5</sup>

## 2.4 Sukuk; Equity or Bonds?

Sukuk is a financial instrument that shares characteristics with bond and stock which are issued to finance trade or the production of tangible assets<sup>6</sup>. Similar to a bond, Sukuk has a maturity date and in some of them the holder will receive a regular income over the period and a final payment at the maturity date. While the conventional bonds price is determined only by the creditworthiness of the issuer, Sukuk price is determined by the creditworthiness of the issuer and the value of the asset. Although Sukuk is also similar to stocks in the sense that it represents ownership and no guarantee of a fixed return (at least theoretically and in the standard model of Sukuk) but stocks have no maturity date. Sukuk also has to relate to a specific asset, project or service.

Sukuk is a relatively infant financial instrument, designed to be a Shariah compliant alternative to conventional bonds, however much debate has been raised on the nature of the instrument, particularly in cases of default, where Sukuk holder designation was confused between equity holders and debtors. There are many reasons behind the confusion; however, some people say that, Sukuk is indeed equity and not a bond. A Sukuk can be structured on a debt based model such as Ijarah or Murabaha, yet certificate holders still are owners of the underlying asset that is leased to the beneficiary. So either the Sukuk is structured on an equity based model where Sukuk holders partner with the originator in a completely new venture or in already existing business or based on a debt based model, the Sukuk holders are always and surely equity holders and not debtors.<sup>7</sup>

There has been considerable debate as to whether Sukuk instruments are akin to conventional debt or equity finance. This is because there are two types of Sukuk:

<sup>5</sup> IIFM Newsletter, March 2017, Issue 1, p.7.

<sup>6</sup> Hakim, S, Islamic money market instruments, in M. Hasan & M. Lewis, (eds), Handbook of Islamic Banking, Edward Elgar Publishing, 2007, pp. 161-171 and Godlewski, C, Turk-Ariss, R, & Weill, L., Sukuk vs. conventional bonds: A stock market perspective, Journal of Comparative Economics, 41, 2013, pp. 745-761.

<sup>7</sup> Sukuk; Equity or Bonds? Available at <http://www.idealratings.com/Sukuk-equity-or-bonds.html>.



- 1) Asset-based Sukuk that is raising finance where the principal is covered by the capital value of the asset but the returns and repayments to Sukuk holders are not directly financed by these assets.
- 2) Asset-backed Sukuk that is raising finance where the principal is covered by the capital value of the asset but the returns and repayments to Sukuk holders are directly financed by these assets.<sup>8</sup> According to being asset backed or asset based, Sukuk can be more similar to bonds or shares so we explain the structure of both of them.

## 2.5 Asset backed-Sukuk

Asset backed-Sukuk involve granting the investor (Sukuk holder) a share of a tangible asset or business venture along with a corresponding share of the total risk (that is, a share commensurate with this ownership). In this structure, there is a true sale transaction, where the originator sells the underlying assets to a special purpose vehicle (SPV) that holds these assets and issues the Sukuk backed by them. The buyers of Sukuk don't have recourse to the originator if payments are less than usual. A true sale implies that the assets of the issuer will not be added to the assets of the originator in the event of default and liquidation. The Sukuk holders must assume any losses in case of impairment of Sukuk assets. Asset-backed Sukuk are, thus, closer to equity than debt and for that reason are not so popular in the market of Sukuk offerings.<sup>9</sup>

## 2.6 Asset-based Sukuk

Asset-based Sukuk on the other hand, involve the issuer purchasing the underlying assets and then investing, trading or leasing them on behalf the investors (Sukuk holders), using the funds raised through the issued certificates (Sukuk). This structure, most often, takes the guise of a sale-lease to the originator and is embedded with a binding promise from the originator to repurchase the underlying assets at maturity. In this structure, the Sukuk holders can only require the originator to purchase the underlying assets. As such, the Sukuk holders have an unsecured debt

<sup>8</sup> Islamic finance – theory and practical use of Sukuk bonds, ACCA, FEBRUARY 2013.

<sup>9</sup> What Is the Difference Between Asset-Backed Sukuk and Asset-Based Sukuk? Available at <http://investment-and-finance.net/islamic-finance/questions/what-is-the-difference-between-asset-backed-Sukuk-and-asset-based-Sukuk.html>.

claim against the originator embodied in the payment of the purchase price following an execution of the binding purchase promise. This implies that Sukuk holders don't have full recourse to the underlying assets and the underlying assets are not used as collateral. Asset-based Sukuk grant only beneficial ownership to the Sukuk holders, so that in case of default, the investor would be left without any claim on these assets. In this structure, the originator typically transfers to the investors only the beneficial ownership of the SPV issuer. But shari'a stipulates a transfer of assets to Sukuk holders. However, since investors have no recourse to the assets, the structure doesn't pay any attention to the asset risk, but rather concentrates on the creditworthiness of the sponsors of the Sukuk.<sup>10</sup>

There are fundamental differences between asset-backed and asset-based Sukuk. The diagrams set out below explain the mechanics of how each Sukuk operates.

**Asset-backed Sukuk:**

It is a kind of financing acquisition of assets or raising capital through sale and lease back like as below:

1. Sukuk holders subscribe by paying an issue price to a special purpose vehicle (SPV) company.
2. In return, the SPV issues certificates indicating the percentage they own in the SPV.
3. The SPV uses the funds raised and purchases the asset from the obligor (seller).
4. In return, legal ownership is passed to the SPV.
5. The SPV then, acting as a lessor, leases the asset back to the obligor under an Ijarah(lease) agreement.
6. The obligor or lessee pays rentals to the SPV, as the SPV is the owner and lessor of the asset.
7. The SPV then make periodic distributions (rental and capital) to the Sukuk holders.

Asset-backed Sukuk certainly have the attributes of equity finance – the asset is owned by the SPV. All of the risks and rewards of ownership passes to the SPV. Hence, should the returns fail to arise the Sukuk

<sup>10</sup> Ibid.

holders suffer the losses. In addition, redemption for the Sukuk holders is at open market value, which could be nil.

**Asset-based Sukuk:**

It is a kind of securitization of leasing portfolio like as below:

1. Sukuk holders subscribe by paying an issue price to a SPV company.
2. In return, the SPV issues certificates indicating the percentage they own in the SPV.
3. The SPV will then purchase a portfolio of assets, which are already generating an income stream.
4. In return, the SPV obtains the title deeds to the leasing portfolio.
5. The leased assets will be earning positive returns, which are now paid to the SPV company.
6. The SPV then makes periodic distributions (rental and capital) to the Sukuk holders.

With an asset-based Sukuk, ownership of the asset lies with the Sukuk holders via the SPV. The payment of rentals provides the return and the final redemption of the Sukuk is at a pre-agreed value. As the obligor is the lessee, the Sukuk holders have recourse to him if default occurs. This makes this type of Sukuk more akin to debt or bonds.<sup>11</sup>

We can summarize the differences of these two types of Sukuk as below table:<sup>12</sup>

| Categories                           | Asset based   | Asset backed  |
|--------------------------------------|---|---|
| Source of Payment                    | The source of payment comes from originator/obligor's cash flows. | The source of payment comes from the revenue generated by underlying asset. |
| Presentation/disclosure of the asset | The asset stays on the balance sheet of originator/obligor        | The asset is separated from the originator's book.                          |
| Type of Sukuk holders'               | Beneficial ownership with no right to dispose                     | Legal ownership with right  |

<sup>11</sup> Islamic finance – theory and practical use of Sukuk bonds, ACCA, FEBRUARY 2013, p.1-3.

<sup>12</sup> Sutan Emir Hidayat, A Comparative Analysis between Asset Based and Asset Backed Sukuk: Which One is More Shariah Compliant?, International SAMANM Journal of Finance and Accounting, July 2013, Vol. 1, No. 2, p.26.

|           |   |  |
|-----------|---|--|
| Ownership | the asset   | to dispose of asset.   |
| Recourse  | Purchase undertaking at par from obligor is the ultimate recourse. The recourse is only to obligor and not the asset. | Sukuk holders only have recourse to asset thus asset plays genuine role in defaults. |

Actually, the asset-based Sukuk were structured as debt instruments on the grounds that “this is what investors were looking for” and because “this is what the market wanted. Another reason for replicating debt-like instruments was that issuers wanted to raise capital without having to sell any assets. Investors, on their part, did not want to become owners of assets and assume the risks of ownership. They wanted bond-like instruments with income and capital guarantees. They wanted their profits to be guaranteed and to earn them without taking risk.

In order to enable both originators and investors to realize their respective objectives, a special type of securitization would accordingly be required. Selling the underlying assets to investors by way of a true sale, as required by the Shariah, would not achieve the respective objectives of the originators and the investors. What was required was a type of sale that would enable originators to “sell” underlying assets to investors and at same time allow them (the originators) to retain legal ownership of the assets thus “sold.” This could be accomplished by utilizing a sale that falls short of a true sale.

However, such a sale is not available in the Shariah. A sale that falls short of a true sale is, however, found in common law, widely known for its creditor friendliness, where it is recognized as a valid sale. Thus, it was necessary to depart from the Shariah on the issue of sale. Common law (practiced in the UK) recognize sales that fall short of true sales as valid sales. A sale that falls short of a true sale allows a “seller” to “sell” an asset and to retain legal ownership of the asset thus “sold” at the same time. Such a sale does not require the transfer of legal ownership from the seller to the buyer; a sale that falls short of a true sale transfers merely “beneficial ownership” on the buyer. In order to accommodate the objectives of both issuers (to retain legal ownership of assets) as well as of the investors (to obtain income and capital guarantees), arrangers thus resorted to the common law instead of the Shariah notion concept of sale. This decision, however, raised a number of

questions. First, was the departure from the Shariah notion of sale justified? Second, how can a departure from the Shariah concept of sale be expected to produce Shariah compliant Sukuk? Third, will investor's interests be adequately protected, given that the sales of the underlying assets give them less than legal ownership of the assets? As a result of a lack of a true sale of the underlying assets by originators to investors, a new class of Sukuk emerged, known as "asset-based" Sukuk. It was this class of Sukuk that was declared non-compliant by the AAOIFI in 2008, just months before the recent global financial crisis. It was in this class of Sukuk that all the defaults took place.<sup>13</sup>

## 2.7 Comparing Asset-based and Asset-backed Sukuk with other Forms of Securities

In this section we deal with this subject that one of the above mentioned forms of Sukuk is more similar to bonds and one of them is more similar to shares. As mentioned before, Sukuk are in two forms of asset-based and asset-backed. In the first type, original capital is guaranteed via tangible or intangible assets of the issuer; and, the profit payable to investors is not necessarily stemmed from a specified asset. However, in terms of the second type, both repayment of original capital and income belonging to the investor is directly resulted from underlying asset ( it should be noted that in terms of the repayment, it is possible if the asset exists and is not destroyed on the maturity date).<sup>14</sup> Therefore, holders of the second type of Sukuk share also the loss. Moreover, in this type due dates for payment of profits are not predetermined; whereas, in the first type a specified amount of profit is paid to the Sukuk holders on certain time intervals, in the second type of Sukuk, the amount of profit depends on earnings resulted from the asset.<sup>15</sup> In fact, original capital and profit belonging to asset-based Sukuk is guaranteed; while, original capital and profit belonging to the holders of asset-backed Sukuk is not guaranteed and they share both the loss and profit. To the same reason, structures of first and second type of Sukuk have been resembled to bonds and stocks, respectively. It should be noted that, shareholders divide the remaining parts of the company's assets among themselves in proportion to their shares, due to the stock's structure. Meanwhile, in

<sup>13</sup> Abdul Karim Abdullah, Asset-backed vs asset-based Sukuk.

<sup>14</sup> Islamic finance-theory and practical use of Sukuk bonds. Available at: [www.webcache.googleusercontent.com](http://www.webcache.googleusercontent.com).

<sup>15</sup> Asset-based vs asset-backed Sukuk, available at: [www.opentuition.com](http://www.opentuition.com).

case the originator becomes bankrupted in process of issuance of asset-backed Sukuk, holder has objective right as to the assets specifically used for such issuance (priority against other creditors); however, because the Sukuk holders will be affected by the loss of the same specific asset in the case of being destroyed or discounting of that asset, these securities may be considered similar to the stocks. Each of Sukuk types, e.g. lease-based Sukuk may be of asset-backed or asset-based type. In asset-based Sukuk, holders are considered as beneficial owners; and, in terms payment of profits is failed, they are entitled to refer to the originator.

By beneficial ownership, we mean some elements of the “ownership right” package such as the right to use the profit from the asset belonging to the beneficial owner; even though, the legal ownership belongs to another person. Therefore, these securities hold a value independent of underlying asset and are considered beyond title deeds. Their meaning is closer to the concept of common bonds; while, they do not represent or prove any specific asset. In asset-backed Sukuk, holders are owners of the asset and in case the originator fails to pay the profit, they are entitled to collect their debts from the asset.<sup>16</sup> Theoretically, Islamic financial system is mostly considered as an asset-backed financial system; connecting each financial claim to a real asset related thereto. In Islamic financial system, each financial claim is considered as a dependent claim, returns or performance of which depends on return or performance of a real undertaken asset.<sup>17</sup> Practically, issuing the most prevailing type of Sukuk e.g. lease-based Sukuk is based on asset-based system, payment of principal and profit is guaranteed and it resembles the structure of bonds in non-Islamic countries. Although holders of bonds are not theoretically sharing loss with the originator and they just receive profit; in case of issuance of Islamic securities, the risk imposed on the holders is removed with the help of insurer institutions and their function is identical to that of bonds, in practice. In non-Islamic countries, asset-backed securities resemble guaranteed debt, i.e. the company puts its own assets (such as financial claims) as a support for loan payment. As a result,

<sup>16</sup> Afshar, Tahmoures A., USA compare and contrast Sukuk (Islamic securities) with conventional bonds, are they compatible?, School of business, Woodbury university, the journal of global business management volume 9, number 1, 2013, p.1.

<sup>17</sup> Vaez Barzani, Mohammad; Dallali Isfahani, Rahim; Al Busuylam, Moslem, “Engineering Islamic financing system”, collection of articles, 2nd International Conference on Development of Financing System in Iran, 2010, p. 235

holders of asset-backed securities have to pay more attention to those assets backing a loan, rather than overall assets of the business.<sup>18</sup>

In asset-backed Sukuk, in case the originator becomes bankrupted, holders of Sukuk have priority against other creditors because their securities represent their objective right towards the asset backing the issuance of those securities.<sup>19</sup> Asset-based Sukuk were foreseen because the issuers were not willing to sell the asset and investors were not ready to accept the risk resulted from asset-backed ownership; they were demanding documents similar to bonds, with fixed incomes. It seemed necessary for the asset-backed to be sold to investors, transforming them to beneficial owners; while the legal ownership still belonging to the issuer. This way, investor would just share the profit stemmed from the asset; which, this kind of ownership is not accepted by Sharia.<sup>20</sup> However, supposing issuance of asset-backed Sukuk, it should be cited that in fact there is still no difference between the two structures (asset-backed Sukuk and bonds); that is, in both cases and if the project is not profitable or the assets are lost, the loss is borne by the investor. The difference is that, in terms of Sukuk, possible dishonoring is already included in the contract concluded between investor and issuer. So, the economic result is the same even if legal analyses in terms of Sukuk may be based on consistency of wills and also sharia. This way, the only difference between asset-backed Sukuk with bonds in conventional term is that Sukuk holders share the loss and profit through contract, in which the buyers of this type of securities explicitly exempt the issuer from payment of profit, in case of bankruptcy.

On the contrary, nonpayment of profit resulted from bankruptcy in terms of conventional bonds depends on an implicit provision. That is, buyers of bonds as reasonable and normal human beings implicitly accept incapability of the issuer to pay the principal or profit in case of bankruptcy; and, knowingly they buy the bonds. So, we may not differentiate between asset-based and asset-backed Sukuk, in terms of economic effects. Again, it should be noted that in Islamic economy and financing, asset-based securities also make the philosophy of these markets to become realized. The reason is that, ownership is a credit-based

<sup>18</sup> Ayotte, Kenneth M., Goan, Stav, *Asset-backed securities: Costs and benefits of bankruptcy remoteness*, 2010, p.3.

<sup>19</sup> Khnifer, Mohammad, *When Sukuk default-asset priority of certificate-holders vis a vis creditors*, University of Reading, ICMA Centre, *Opalesque Islamic finance intelligence*, No.11, 2012, p.1

<sup>20</sup> Abdullah, Abdul Karim, *Asset-backed vs asset-based Sukuk*, 2012, p.2

relationship and what difference it makes for an individual's ownership to be based on tangible, or intangible and nominal assets? <sup>21</sup>

## 2.8 Differentiation Aspects of Sukuk and Bonds

Similarities of Sukuk and bonds may be considered as their liquidity in secondary market, their credit being rated by rating agencies and variety in their design and supply. However, it has been told that Sukuk differ from common bonds of financial markets in seven aspects. This section will explain these differentiation aspects.

Firstly, Sukuk are indicative of ownership to a certain asset; while, bonds are just indicative of a debt obligation, i.e. the relationship between the issuer and purchaser of bonds resembles the relationship between the lender and borrower. Issuance of bonds is backed by money (outstanding claims); while, Sukuk are issued through support of tangible and real assets. Of course, apparently the relationship of people with tangible assets is based on ownership; but, this is not so in practice. Sukuk owners have no interference in the process of managing and control of the asset; they are not informed of the issuer's calculations. The result in general is that, there is a possibility for efficiency of the Sukuk to be decreased. <sup>22</sup>

Secondly, the subject assets of Sukuk shall be authorized and tangible upon sharia definition; whereas, securities could be backed by intangible assets and even those assets not accepted by Islam. Thirdly, validity of securities depends on and is measured through credit of its issuer; whereas, validity of Sukuk depends on value of the assets backing it. Therefore, if we analyze Islamic securities upon the underlying asset, the buyer shall make some expenses to investigate if the holder is really the owner of the Sukuk (indication underlying asset) or not? Moreover, the buyer has to check for the underlying asset to see if it is wasted and if its real value matches the value of the Sukuk he is buying, or not.

Forth, selling Sukuk in secondary market is similar to selling the ownership of an asset. However, selling bonds is considered as selling an "ownership right" package which has value by itself. The fifth difference is: Sukuk are apparently a type of contract and civil partnership which results in joint ownership of people over underlying assets. Of course,

<sup>21</sup> Shushi nasab, Nafiseh, **legal nature of securities**, 2015, p.152.

<sup>22</sup> Barzel, Yoram, *Economic analysis of property rights*, Second edition, Cambridge cb21rp, United Kingdom, Cambridge University press, p.12.



this kind of structure of Sukuk ownership justified in form of civil partnership will be followed by reduction of economic efficiency of these securities. For example, in civil partnership it is important that how well the partners know each other, because these kinds of partnerships are considered as the individual's company. Whereas, those people who buy Sukuk don't know each other and have to pay for such identification. This increases transaction costs and is considered as a threat to economic efficiency of these securities. The problem implies wherever partnership in physical asset is arisen.<sup>23</sup>

Of course, as mentioned before, Sukuk are only theoretically of contractual basis and considered as a title deed. In practice, they are not described as an ownership because the holders have no right to possess, partition or manage the underlying asset; and, they have no voting right to decide on the asset-related issues. They are just entitled to receive principal and forecasted profit for the security. So, it could be suggested that, these securities are born through contract and transacted in form of a package for ownership rights.

Sixth, holder of Sukuk shares the profit and loss of the issuer; whereas, holder of bonds just shares the profit. However, in the section titled 'Difference between asset-base and asset-backed Sukuk' we have mentioned that from this point of view they are not different, because profit of Sukuk holders also is guaranteed. It has been told that, Islamic securities have some similarities to conventional bonds in terms of operational method. However, in terms of content and nature, they are basically different. Conventional bonds are usually designed according to a contract of loan with interest; holders have no right as to the ownership of real assets and economic activities and profit resulted there from; they just receive a fixed or sometimes variable interest on due dates. In cases of Islamic securities, holders share the ownership of real assets and economic activities; and, any profit from projects and activities affects them. In this case, profit is affected by real section of economy.<sup>24</sup> However, contrary to what were theoretically considered as desirable in invention of Sukuk, i.e. dividing profit and loss together; the issue did not come to practice. This is why; it has been told that in the process of issuing Sukuk, the same conventional bonds are offered to public, labeled as

<sup>23</sup> Farooq, Mohammad Omar, Partnership, Equity-Financing and Islamic Finance: Whither Profit-Loss Sharing?, Review of Islamic Economics, Vol.11, special Issue,2007, p.67.

<sup>24</sup> Taskhiri, Mohammad Ali, "Sharia-defined foundations of Islamic securities (Sukuk)", Islamic Economy quarterly, vol.7, No.27, 2007, p.1

“Islamic”.<sup>25</sup> It was mostly believed that interest-based system of bonds will be replaced with profit-loss sharing system (PLS), however, in Sukuk also theoretically the parties share in profit and loss, but in practice if the project is profitable, investors receive just an amount as profit and in case the business bankruptcy, financial risk will only be imposed on investors; and, the business just loses its workforce.<sup>26</sup> It is the same as what happens in case of bonds. To the same reason, in financial market crisis in 2008 which resulted in the securities markets crash, those markets relying on Islamic securities were also affected<sup>27</sup> because Sukuk has been considered as a copied form of conventional bonds not as a real and standard asset-backed Sukuk, by many.<sup>28</sup>

The seventh difference is that, issuance of bonds imposes the risk on the borrowing institutions; while, the system for issuing Sukuk (asset-backed Sukuk) imposes the risk on investors and financing parties. The results from a study show that, total imposed risk in the latter case is more than the total risks stemmed from bankruptcy of those who issue bonds.<sup>29</sup> Issuers of Sukuk also transfer the risk to insurers, through insurance contracts. So, no difference exists between the two securities, in this respect also. This way, the difference in structure of these two categories of securities is more theoretic and economically there is no fundamental difference between the two. In Sukuk structure (asset-based Sukuk), holders of these securities are beneficial owner of the underlying asset. These securities represent proportional and simultaneous ownership of existing asset or a collection of various assets that are considered as collateral against current or future cash flows derived from these assets, during a certain time period.<sup>30</sup>

### **2.8.1 Concept of Converting Assets to Securities (securitization) in Terms of Sukuk**

The purpose of this section is to clarify securitization process in Sukuk structure. As we know, conversion of assets to securities makes those commodities, claims, or credits incapable of becoming cash, or those

<sup>25</sup> Farooq Mohammad Omar, Op.Cit, p.67.

<sup>26</sup> Ibid, p. 68.

<sup>27</sup> Norman, Trevor, Sukuk: Where next?, Newhorizon, 2009, p.14.

<sup>28</sup> Abdullah, Abdul Karim, Op.Cit, p.2.

<sup>29</sup> Hesse, Heiko, Jobstandreas, Sole, Juan, Trends and challenges in Islamic finance, Word economics, Vol.9, No.2, 2008, p.182.

<sup>30</sup> Afshar, Tahmoures A., Op.Cit, p.1.

which are potentially unusable, to become convertible to securities and also transferrable, accordingly.

Conversion of assets to securities enables minor investors to buy small parts of the asset without being enforced to pay entire price of the overall asset for its purchase.<sup>31</sup>

Contrary to guaranteed debts, converting assets to securities means transfer of ownership of the asset to a SPV, which the latter subsequently sells his related right over the assets to the investors, against cash payment. In fact, converting the assets to securities is an organized process upon which, loan interests or other receivables and claims are packaged and underwritten; then, they would be sold in form of asset-backed securities. The process enables investors to allocate the capital more efficiently and find access to variable resources with less cost, primarily.

Then, the process leads to liquidity or improving it. In other words, conversion to securities is a process during which, the assets belonging to the owner or the originator will be extracted from the balance sheet. In turn, financing would be made by those investors who buy a tradable financial instrument; the instrument represents such a debt, with no reference being made to the first lender. Process of converting the assets to securities makes the companies' procedure of investment, more efficient. In the process, when the company's assets are backing issuance of securities or Islamic securities and the asset is converted to securities; securities become valuable and could be transacted in primary and secondary markets. The asset may be the company's loan or mortgage assets.

In Islamic financing system, generally in process of converting assets (including mortgage loans) to securities, the company or institution in need of financing establishes a SPV, SPE, or SPC and sells to it those of its assets which have perspective cash flows. The SPV issues asset-backed securities to provide money required for the purchase of aforementioned assets and the securities are sold to all of the investors. Then, the latter pays to the originator, the fund obtained from selling the securities, for purchase of financial assets. Those investors, who have bought asset-backed securities, obtain profit from cash flows stemmed from financial assets of SPV.

<sup>31</sup> Merritt, Cam, What Is the Meaning of Securitization? Available at: [www.homeguides.sfgate.com/meaning-securitization-6615.html](http://www.homeguides.sfgate.com/meaning-securitization-6615.html).

### **2.8.2 Concept of Asset in Terms of Sukuk**

Underlying assets are different in terms of bonds, comparing to Sukuk. In general, what the term “asset” suggests in issuance of bonds including material and immaterial properties, concerns outstanding claims or cash acting as a support and guarantee for issuance of such bonds. “Asset” in the process of issuing Sukuk (asset- backed Sukuk) suggests tangible assets converted to these types of securities possessed by Sukuk holders; while, this is not considered as collateral for the principal and the profit resulted there from. This way, asset belonging to the issuer of conventional bonds which is considered as a base for such issuance is called “underlying asset”, because it forms the basis for the issued bonds. However, the issued bonds will be separated from underlying asset and no longer explain it. Whereas, in Islamic financing and in terms of Sukuk (asset- backed one), underlying assets are considered as the basis for issuance of Islamic securities and Sukuk are exactly considered as the title deed and explain that kind of asset. For example, in ijarah (lease-based) Sukuk, underlying assets are those assets sold to the SPV, based on which the SPV issues Sukuk and Sukuk holders are considered as direct owners of the underlying asset. The asset is the so called “underlying asset.”<sup>32</sup>

### **2.8.3 Concept of SPV (special purpose vehicle) in Sukuk: The Difference between SPV as an Intermediary in the Process of Issuance of Sukuk and the Concept of Intermediary in Conventional Bonds**

Financial intermediaries are a large part of financial structure formed to reduce conversion costs and to make depositors, loan takers and minor investors capable of benefiting from financial markets. Traditionally, intermediaries for securities are those legal entities assigned to keep securities belonging to the investors, in their electronic systems; sometimes, they become the owner themselves. The latest concept is related to the concept of intermediary in indirect system of ownership. In direct system of ownership, the intermediary which is different from the intermediary institution in the system of issuing Islamic securities, will not be legal owner of securities and just is assigned to keep them.

Concept of SPV in case of Sukuk is different from the concept of intermediary including brokers and depository corporations. As an agent

<sup>32</sup> Shushi nasab, Nafiseh, Legal nature of securities, 2015, p.298.

for issuance of various kinds of Sukuk, SPV is the only institution capable of such issuance. The originator intended to issue securities for its own financing, has to do it just through the SPV. The SPV plays reciprocal role of a proxy. From one side, it is considered as a proxy to the originator for some issues; and as for some other issues, he acts as a proxy to the security holders. It acts usually in behalf of originator before issuance of Sukuk and in behalf of investors after issuing and transferring Sukuk to investors. Although no separate mandate is concluded between the SPV and the originator as to the performing the originator's activities, such issues as contracting sale agent and market maker, or acting as an underwriter obligator implies assignment of some sort of implicit proxy to the SPV, by the originator. After transfer of securities to the investors, SPV introduces itself as a proxy to Sukuk holders in terms of concluding contracts related to the underlying asset; while, it transfers the Sukuk to their holders. This authorizes the SPV to take action regarding concluding such contracts as purchase, lease and guarantee contracts, etc. after issuance of Sukuk. SPV takes action also for receipt and distribution of profit among Sukuk holders, in proportion to the principle.

#### **2.8.4 Difference of Sukuk and Common Bonds, in Case of Bankruptcy of the Intermediary**

In indirect holding system we may encounter risk of bankruptcy of intermediary, this section explains that in Sukuk and supposing bankruptcy of intermediary, this risk does not exactly exist because the holding in Sukuk system is mostly direct not indirect.

As we know, the effect of separating direct and indirect holding would be brought up, supposing bankruptcy of the intermediary. That is, supposing bankruptcy of intermediary, whether intermediary creditors have priority over customers or not? Many Roman-Germanic law countries have not answered to the question. Korea, Japan and Germany are considered as few civil law countries, having some regulations in this respect. In Korea, the issue has been referred to "Securities and Exchange Act". Accordingly, the customer is known as the ultimate owner of securities, instead of intermediaries.

The same provisions have been provided in separate legislations, in Japan and Germany. So, in case of bankruptcy of the intermediary, customers have priority against creditors of intermediary. Unlikely, some people believe that where no explicit Act exists, no assertion could be

made in terms of priority of customers.<sup>33</sup> It seems that a separation should be made: when the intermediary does not benefit from those securities in his possession, customers have priority against creditors of intermediary, because the intermediary just acts as a trust and holder of securities. However, in those cases that the intermediary is the real owner of securities, this could not be asserted that customers are prior to creditors of intermediary. It goes without saying that, in this case intermediary's creditors have priority against customer, because intermediary possesses the securities and any legal rights stemmed from. However, some people believe that in indirect system of ownership which intermediary is the legal owner and customers are considered as real owners of securities; necessarily, the law shall set the obligations in this respect. In case of bankruptcy of intermediary, we may not suppose customers have priority against creditors to the intermediary.

The problem does not exactly imply for Islamic securities, because from among rights and obligations set for intermediary institution (SPV), we may also refer to selling and renting those assets belonging to the Sukuk owners, as the case may be. However, the institution has no simultaneous ownership with holder of securities over assets, so that; any probable claim by another person or creditor except for the Sukuk holders would be prevented. So, no dispute arisen between creditors of intermediary institution (SPV) and Sukuk holders would be probable. Of course, in case Sukuk has been foreseen in an indirect system of holding, these bonds bear also the same problem and aforementioned solution for conventional bonds is applicable, too.

The question may arise that in case of bankruptcy of the originator, which one of the originator's creditors or Sukuk holders holds priority? The answer is that, to convert assets to securities through issuance of Sukuk, eligible assets have to be first separated from original company and transferred to special purpose vehicle/entity (SPV). This is usually a limited liability company. Transferring the asset to the SPV takes away all asset-based risks from the original company; while the risks are transferred to SPV. Moreover, Sukuk holders also become sure that all asset-based rights belong to them and no other person would be liable to any claim in this respect. However, if the asset had been included in balance sheet of the original company and not transferred to a SPV; then, credi-

<sup>33</sup> KonSik Kim, a civil law jurist's perspective on intermediary risk in the indirect holding system for securities: a comment on schwarcz & Benjamin, 2002, pp.335-339.

tors to the originators also may have been claimed those assets.<sup>34</sup> Again and as an example in lease-based Sukuk, Sukuk holders have objective rights as to the underlying asset and Sukuk are theoretically considered as a title deed, therefore, arising dispute between creditors to the originator and Sukuk holders is basically denied.

### **2.8.5 Comparing Concept of Ownership in terms of Sukuk and Indirect Holding in Conventional Bonds**

In this section, we aim to show some similarities between ownership of bonds in indirect holding system and ownership in Sukuk system.

In process of issuance of Sukuk, SPV as a trust (commission agency) is established to own the assets and holders of these financial certificates have only joint benefit in what the trust owns as the assets. In other words, an SPV works as a commission agency, i.e. buys an asset in its own name as nominal owner and to the benefit of customers; while, it sells the asset in its own name and to the benefit of customers. In fact, there are benefits from the asset which are sold, because the asset itself never would be possessed by investors.

The procedure is exactly similar to indirect holding of common bonds. In the process of issuing Sukuk, the intermediary institution (SPV) as a commission agency on behalf of the originator is commissioned to sell his asset; and on the other side, as a commission agency on behalf of investors is commissioned to buy underlying assets to their benefit. Since the price of such asset is valued upon the market value and not mutual agreement of the parties, the commission agency (SPV) is authorized to possess the asset as a buyer and then to sell the same asset to the investors, through issuance of Sukuk. As it could be observed, the intermediary agency performs almost the same functions done by the trustee in trust and works as an intermediary between investors (financial suppliers) and the originator (issuing institution). This forms the nature of indirect ownership (holding), i.e. a relationship based on intermediating between the issuing party and the investor. The Sukuk system is just one step behind indirect ownership; in a way that, physical bonds would be possessed by the investors and the commission agency (SPV) has no

<sup>34</sup> Pahlavan, Hamid; Razavi, Sayyed Ruhollah, "Sukuk (Islamic securities), definition, types and structure, management of Islamic researches and studies, Securities and Exchange Organization of Iran, p.27.

responsibility for custody of securities, which in near future would be resulted in paperwork crisis.<sup>35</sup>

To explain exactly the difference between indirect holding system in those countries issuing common securities and those countries engaged in issuance of Sukuk, we have to study similarities and differences existing between the two:

In Islamic system of issuing securities, Sukuk represent underlying assets; however, in those systems issuing common securities, these securities represent the value of underlying assets owned by the issuing company. Both systems use an intermediary institution in respect of setting up a relationship between investors and the institution in need of financing. Owners of Sukuk may sell them and the amount they receive in return is equal to the value of underlying asset, at the time of selling the bond. Owners of securities in those countries following indirect holding systems also may sell ownership of profits and the amount obtained in return would be equal to the value of underlying asset of the company, at the time of selling securities.

Ownership of holders of securities in neither system is considered as complete, i.e. they just are owners of the effects of ownership such as the right to receive related profit. For example, in none of the two systems, owners of securities have the right whatsoever to possess the underlying asset.

As you may notice, real effects and nature of ownership in both systems issuing Sukuk and common securities is similar; however, they differ in appearance. But, it should be noted that legal world deals with the intent and not the external aspects. The only difference existing between the two systems in terms of method of ownership of securities could be summarized in one point: holders of securities in non-Islamic countries have no right whatsoever as to the possession of the securities. They are just real owners of benefits resulted from these securities, i.e. they are entitled to receiving profits; and, the intermediary institution holds securities in electronic form. However, holders of Sukuk have them in their possession with no right to possession or division of the underlying asset.

This is exactly the same point stimulating those countries issuing Islamic securities to foresee indirect holding system, because material possession of Sukuk in near future will lead to paperwork crisis (e.g. Ameri-

<sup>35</sup> Shushi nasab, Nafiseh, Legal nature of securities, 2015, p.312.



ca, 1969), due to public interest in performing transactions through Islamic securities. So, our proposition is that these bonds also would not be possessed by their holders and precise systems would be made just available to the SPV or other intermediaries such as central depository corporations to keep them in electronic form; and, holders of Sukuk only benefit from their profits.

Therefore, similar to DTCC (Depository Trust and Clearing Corporation) in America being located at the head of intermediaries' hierarchy and having a legal entity within itself as Cede & Co., we may also apply such an approach in those countries where Sukuk are issued. That is, depository corporations in these countries act as a mother company and create an institution of legal entity affiliated to themselves, so that; the institution be enabled to possess and keep the issuers' securities in electronic form and then to sell the right stemmed there from to the investors. This way, the bond issuers sell their Sukuk to the depository corporation in form of large blocks; then, this depository corporation sells the Sukuk to brokers and other investors, in form of smaller blocks. In such a case, we may say that electronic Sukuk are primarily bought by the depository corporation as a brokerage and kept by the same corporation, after being sold to the holders.

It should be noted that, in case an indirect holding system for Sukuk is foreseen, the ownership shall be justified according to the brokerage institution; because, in Islamic countries just like those countries with civil law, simultaneous ownership of an asset is not accepted.

However, if the issuer country is within the common law countries such as England, the ownership will be definitely justified based on trust and simultaneous ownership of SPV (as legal owner) and investors (as beneficial owner); this way, Sukuk will be owned by a legal and beneficial owner, at a time. Therefore, in case electronic Sukuk and establishment of indirect holding of them is foreseen, these bonds could be justified differently based on the issuer country, i.e. in those countries conforming with civil and Islamic law, according to brokerage; and in common law countries, on the bases of trust and simultaneous ownership.

### **2.8.6 Comparing Registered and Non-Registered Sukuk with Other Securities in This Respect**

Securities may be divided into two forms of registered and non-registered securities, in terms of their method of transfer through taking

delivery and handing over, or booking. In case of non-registered securities, ownership is transferred through taking over the physical form of bonds; however, in case of registered securities, ownership is registered and transferred in electronic form. Sukuk will follow the same pattern of division. Sukuk being registered or non-registered is related to the type and nature of these bonds. For example, lease-based Sukuk are not currently issued in non-registered form; because, they represent joint ownership of the person in underlying assets. Therefore, at the time of their transfer in the secondary market, buyer and customer shall be specified and they could not be transferred through taking delivery and handing over. Whereas, some other types of Sukuk may be issued in non-registered forms, including “partnership-based Sukuk”. These types of Sukuk are those financial certificates of identical value, used for accumulation of funds necessary for setting up new projects, development of current ones, or financing for partnership-based businesses. Those people holding Sukuk, are considered as the owner of project or its assets in proportion to their share from partnership. Partnership-based Sukuk could be transacted through taking delivery and handing over.

### **2.8.7 Sukuk-Related Challenges in Comparison to Conventional Bonds**

Accepting the perspective which considers Sukuk as being asset-backed, one of the challenges issuance of Sukuk would be confronted with is that underlying assets for issuance of Sukuk have to be tangible; although, selection of the same tangible assets is also restricted. The same problem results in lowering speed of financing procedure of the companies and makes us to believe that although Sukuk are considered as an invention in Islamic domain of financing; they do not have functions of bonds, economically.

Of course, some people believe that Sukuk are basically different from bonds and in fact, a third type of securities; something in between of stocks and bonds. These groups consider inefficiency of Sukuk to be stemmed from failing to observe existing standards, in their issuance. The difference between ideal Sukuk with those issued in reality is to the level that according to a report (2008) by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), 85% of issued Sukuk (till 2008) have failed in observing defined related standards. For example, legal ownership of the assets has not been transferred to the Sukuk buyers. The reason is that real Sukuk have no economic efficiency

for the issuers, which makes them close to conventional bonds. For example, considering lease-based Sukuk (*al-ijarah*), we may see that they are designed in a way that the holders receive an amount as rental on due dates.

However, in reality the amount by no means reflects the rental from the subject asset of Sukuk; rather, it is the interest rate of what has been invested by the buyer for purchase of these bonds or for example if the assets considered as a base for issuance of Sukuk are two different assets, commonly in the market two different rentals are supposed to be specified, however, it is observed that the amount is identical for various Sukuk based on different assets; and, the basis for specifying it becomes close to the interest rate. Such an approach is problematic in terms of the market economy. For instant, in those conditions that an immovable property is the base for issuance of Sukuk and related rental increases; there is a possibility for profit of the holders to be reduced just because of decrease being made in interest rate of international markets.<sup>36</sup>

Another presupposition concerns the case that the value of the asset used as the base for issuance of Sukuk is fluctuated and may be decreased, which should normally affect and reduce the rights of holders of Sukuk; however, it is observed that their profit remains intact. Another challenge related to the issuance of Sukuk (asset-backed Sukuk) is the point that contrary to non-islamic securities, underlying assets of lease-based Sukuk are necessarily tangible assets such as immovable properties or other assets; whereas, non-Islamic securities may be backed by intangible assets, including outstanding claims of the company. On the other side, payment of rental as profit and the obligation to redeem the property is considered as a guarantee for repayment of principal amount of Sukuk. However, the problem with these assets is lack of variety; while, the originator may be willing to replace underlying assets with some other assets. A solution foreseen in this respect is that the parties may agree upon all or part of the assets forming the basis for Sukuk to be convertible in certain conditions, upon the originator's recognition.<sup>37</sup>

<sup>36</sup> Al-Bashir, Muhammad, Al-Amine, Muhammad, *Sukuk Market: Innovations and Challenges*, Islamic Economic Studies, Vol.15, No.2, 2008, p.8.

<sup>37</sup> *Ibid*, p.9

## 3 Sukuk Is a New Type of Hybrid Securities

In this part we are going to deal with the Sukuk as hybrid securities. In other words, we are intended to explain that maybe Sukuk are those types of securities which are categorized neither as common bonds, nor stocks. Instead, they are considered as a third type of securities, like hybrid securities in Western countries. So, following the comparison made previously between Sukuk, bonds and stocks, we are going to compare Sukuk and hybrid securities in this section and to introduce Sukuk as a new type of these securities.

### 3.1 What is a Hybrid Security?

Hybrid security<sup>7</sup> is a generic term used to describe a security that combines elements of debt securities and equity securities. Hybrid securities typically promise to pay a rate of return (fixed or floating) until a certain date, in the same way debt securities do. However, they also have equity-like features that can mean they provide a higher rate of return than regular debt securities. In some cases, this is because they give the holder an option to convert the hybrid securities into equity securities (typically ordinary shares), which will give the holder an ‘equity-kicker’ if the underlying equity securities perform well. In other cases, it may be that the hybrid securities have equity-like risks attached and the issuer has to pay a higher rate of return to compensate investors for those risks.<sup>38</sup>

New types of hybrid securities are being introduced all the time in an attempt to meet the needs of sophisticated investors. Some of these securities are so complicated that it is difficult to define them as either debt or equity. In addition to being difficult to understand, another criticism of some hybrid securities is that they require the investor to take more risk than the potential return warrants.<sup>39</sup>

### 3.2 Sukuk and Hybrids

Upon the research findings, we believe Sukuk to be maybe new hybrid instruments. That is, they bear features of both stocks and bonds. For

<sup>38</sup> Understanding Hybrid Securities, Available at: [www.asx.com.au/documents/products/Understanding\\_Hybrid\\_Securities.pdf](http://www.asx.com.au/documents/products/Understanding_Hybrid_Securities.pdf).

<sup>39</sup> Hybrid Security, Available at: <http://www.investopedia.com/terms/h/hybridsecurity.asp>.

example, asset-backed Sukuk like stocks are considered as a type of partnership; and, as the shareholder owns a part of the company as an asset, holder of Sukuk becomes also the owner of a part of an asset or a partner in a project. From this perspective, Sukuk are similar to stocks. On the other hand, Sukuk could be of both registered (like lease based Sukuk) and non-registered (like partnership-based Sukuk) forms, just like stocks. But, on the contrary to stocks, even if theoretically holder of Sukuk owns the asset; he has no voting right as to the asset or project-related decision makings.

Moreover, asset-backed Sukuk holder benefits from priority right against other creditors, in case of liquidation or bankruptcy of Issuer company; and, he may collect his principal capital from related asset, before other creditors. While, this is not the same with stocks and shareholder is entitled to his capital from what has been remained from the asset, after settlement made with all of the creditors. Sukuk system is based on profit and loss like stock system, i.e. like the shareholder, Sukuk holder would be also theoretically sharing profit and loss. Therefore, maybe we could say that if Sukuk holder practically shares profit and loss, Sukuk just like stocks would be a costly method of financing for investee. Because, he has to share the obtained profit with Sukuk holders, like what takes place in terms of stocks. Of course, in recent years we are more observing payment of a fixed profit to Sukuk holders just like bonds; and, they are not sharing real profit and loss of the asset or project, in practice.

On the other hand, at least theoretically and in asset-backed Sukuk also investor is more at risk because of sharing the loss as it is the case with the stocks, comparing to other methods of investment. However, practically the risk is covered via different methods, including insurance. In terms of bankruptcy risk, asset-backed Sukuk are of the minimum risk for the issuer just like stocks because, theoretically it is not a bond with fixed income; instead, it is a kind of partnership in the asset or project ownership. So, in case of sudden bankruptcy of business owned by the issuer, the risk resulted from loss of that asset is imposed on Sukuk holder as an owner to a part of it, just as this is the case with stocks and related shareholders bearing the risk. It goes without saying that, in case the underlying asset is not lost; Sukuk holder is of priority right for receipt of his principal capital from the asset, in relation to other creditors. Due to various reasons, Sukuk are also similar to bonds. For example, although theoretically they are of no specified and fixed profit, in prac-

tice some of them (asset-based Sukuk) are very similar to bonds and investors usually receive a fixed profit. Like bonds and contrary to stocks, Sukuk bear due dates. Although, the instrument is indicative of some sort of partnership and ownership of the holder in respect of the asset; like bonds, it lacks right of voting and interfering in underlying asset. Apparently, ownership of Sukuk holder is not real and practically like the holder of bond, he is a creditor rather than an owner of the asset or partner thereto, at least in asset-based Sukuk. In terms of tax rules and regulations, Sukuk like bonds need to be exempted from tax. They could not be treated like stocks and be liable to tax payment, just because of partnership in ownership. In other words, they have to be dealt with like bonds, in this respect.

Currently, most tax systems around the world are structured to handle conventional bonds, but lack some of the specific attributes necessary to work with Sukuk and other Islamic financial instruments.

There are several reasons why the appropriate legal structures are necessary for the use of Sukuk. These types of Islamic securities usually involve multiple transfers due to the nature of how they are backed by real assets rather than working on the basis of interest. Legal structures that are not designed to handle this will tax every transfer, creating an unsustainable situation for those involved in the Sukuk transaction. The main reason for this is that Sukuk often require that ownership of the asset covered by the Sukuk be transferred repeatedly from one party to another. Ownership of assets in many regions requires additional tax duties and often involves other legal transactions that incur additional costs.

In the Sukuk structure, when the asset is transferred to the SPV issuer from the originator and moved back, there will be transfer of legal ownership and beneficial ownership of the underlying asset. In Common law systems, the law recognizes that only beneficial ownership is transferred to Sukuk holder when the asset moves and legal ownership is retained by the originator (original owner of asset). Therefore, the asset is not double-taxed with one legal owner. On the other hand most Civil law regimes do not have a separate ownership concept.<sup>40</sup>

<sup>40</sup> Tariqullah Khan and colleagues, *Legal and Regulatory Issues in Issuing Sukuk in Muslim-minority countries: Lessons from Developed Countries' Experience*, p. 11.

Without special provisions for Sukuk, this characteristic of Islamic financial instruments puts them at a severe disadvantage if the right legal frameworks do not exist. A typical example is an Ijara Sukuk structure. In these cases, the initial transfer of asset ownership can trigger capital gains, sales tax, holding tax and stamp duty. Each time a transfer of ownership occurs, which will happen at least twice, these taxes would be required, unlike conventional bonds which would only be taxed according to their capital gains. One hurdle when creating the necessary legal framework for Sukuk in a country's legislation is the differential treatment between profit and interest. Most of the time, interest payments are tax deductible. On the other hand, profit is taxable and Sukuk is based on profit-loss system. In 2010, the United Kingdom, France, Luxembourg and Ireland issued tax neutrality laws that ensured that Sukuk transactions would be tax neutral with conventional bonds.<sup>41</sup>

### 3.3 Different Types of Hybrids and Comparison to Sukuk

As mentioned previously, there are three broad categories of hybrid securities:

1. Convertible/convertible debt securities;
2. Preference shares; and
3. Capital notes.

#### 3.3.1 Convertible/Convertible Debt Security and Sukuk

A convertible debt security is one that gives either the investor or the issuer the option to convert it into another type of security at a specified date in the future. Often this will be ordinary shares in the issuer. We want to notice that Sukuk can be convertible too, means that we have some Sukuk called convertible or exchangeable Sukuk. This security is a type of Sukuk structure in which Sukuk certificates have an embedded option giving the Sukuk holders the right, without the obligation, to exchange Sukuk into real assets.

Sukuk holders can convert their current holdings into a number of pre-determined amount (value) of real assets after a specific period of

<sup>41</sup> See more at: <https://www.Sukuk.com/article/Sukuk-taxation-legal-structures-2332/#sthash.F8waPFyg.dpuf>.

time. Conversion is typically subject to preset conditions (e.g., lock-up period after subscription). Exchangeable Sukuk are instrumental for investors who seek to protect their position in Sukuk- i.e., against unsecured periodic distributions. These investors can walk away from the Sukuk contract by exchanging their Sukuk holdings into real assets currently created or owned by the originator. The exchange (conversion) ratio depends on the current price of the Sukuk. For example, if the Sukuk price is less than the underlying asset price, the Sukuk holders may choose to exchange and vice versa. Exchangeable Sukuk allow Sukuk holders to react to unfavorable economic conditions affecting their Sukuk holdings.<sup>42</sup>

As we can see convertible Sukuk is like convertible bond and as investors can avoid risks of reduction of share price and enjoy increase of that through convertible bonds, they can enjoy the Sukuk and convert them to the asset on the downside of Sukuk price through convertible Sukuk. So these Sukuk can be attractive for investors. As well as we have another type of Sukuk called contingent convertible (CoCo) Sukuk. It is a type of Sukuk structure in which Sukuk certificates give the Sukuk holders a contingent right to convert their holdings into equity. contingent convertible Sukuk become convertible if the price (value) of the issuer's equity rises a certain amount, from the date of Sukuk issuance. Coco Sukuk is somewhat similar to convertible bonds because they can be exchanged to equity but opposite to convertible bonds, they are not optional but are contingent to increase of the share price to determined amount.

### **3.3.2 Preference Shares and Sukuk**

Preference shares, more commonly referred to as preferred stock, are shares of a company's stock with dividends that are paid out to shareholders before common stock dividends are issued. If the company enters bankruptcy, the shareholders with preferred stock are entitled to be paid from company assets first. Most preference shares have a fixed dividend, while common stocks generally do not. Preferred stock shareholders also typically do not hold any voting rights, but common shareholders usually do.<sup>43</sup>

<sup>42</sup> Available at: <http://www.investment-and-finance.net/islamic-finance/e/exchangeable-Sukuk.html>

<sup>43</sup> Read more at: <http://www.investopedia.com/terms/p/preference-shares.asp>



Among different hybrid securities, we think that simple Sukuk (called Plain Vanilla Sukuk) that are without any additional features such as option to convert or exchange into equity at a certain time, are much more like preference shares. Sukuk confers on Sukuk holder a right of ownership to the underlying assets. This is the central aspect of Sukuk's share-like characteristics. Under this circumstance Sukuk holders become an owner of the underlying asset or project<sup>44</sup>, the holders of Sukuk do not have voting rights, just like most of preference shares. Preference shares usually have maturity date and Sukuk have maturity date too.

Like holders of preference shares, asset-backed Sukuk holders are entitled to a payment of value of the Sukuk according to price of the underlying asset in the market and ahead of any distribution or payment of surplus assets to others. It is necessary to notice that there is also a type of Sukuk named senior Sukuk which has features like preference shares, it is a type of Sukuk structure in which Sukuk holders get paid in full before other claim holders. This is because the "senior" Sukuk holders have a high-ranking claim over the underlying assets in the event of default or redemption. Seniority means the Sukuk holder's claims rank superior vis-à-vis others against the issuer and the Sukuk holders of the same rank have similar rights and rank *pari passu* among themselves.<sup>45</sup>

### **3.3.3 Capital Notes**

Capital notes are debt securities that have equity-like features attached. Examples include: Perpetual debt securities, Subordinated debt securities and Knock-out debt securities.

#### *3.3.3.1 Perpetual debt securities and Sukuk*

These are debt securities with no fixed maturity date. They are regarded as hybrid securities because they are a debt security with equity-like features (like a share, they don't mature). These hybrids are comparable to perpetual Sukuk. It is a Sukuk issue that does not mature and hence Sukuk are treated as equity rather than debt. Perpetual Sukuk have no fixed maturity date (final redemption date) and are viewed as part of capital.

<sup>44</sup> Securities Commission Malaysia (SCM), Sukuk, Sweet & Maxwell Asia, 2009, p.19.

<sup>45</sup> Available at: <http://www.investment-and-finance.net/islamic-finance/s/senior-Sukuk.html>

Sukuk holders cannot redeem their certificates (Sukuk) unless a redemption trigger event occurs. In case of redemption, Sukuk may be redeemed in whole but not in part. Perpetual Sukuk have the features of “permanence” and “loss absorption” which means the Sukuk carry a perpetual legal tenure and subordinated to debt and other liabilities of the issuer of such perpetual Sukuk. Perpetual Sukuk are innovative form of debt instruments (from a legal standpoint) with equity-like features that typically ranks senior only to common equity.<sup>46</sup>

### *3.3.3.2 Subordinated debt securities and Sukuk*

These are debt securities whose rights with respect to payment of interest and repayment of principal rank behind (are subordinated to) another class or classes of debt. There is also a kind of Sukuk called subordinated Sukuk. That is a type of Sukuk structure in which Sukuk certificates give Sukuk holders residual claim over the assets financed by their funds. This claim ranks after the claims of other creditors and unrestricted profit sharing investment accounts<sup>47</sup>(UPSIA). Contrary to the conventional sense of subordination, subordinated Sukuk do not represent creditor claims that rank after those of other creditors as this would be inconsistent with shari'ah principles and precepts. Subordinated Sukuk allow Islamic banks to strengthen their Tier 2 capital.

### *3.3.3.3 Knock-out debt securities and Sukuk*

These are debt securities that give the issuer or a third party (such as a prudential regulator a right to extinguish them under certain conditions. they are regarded as hybrid securities because they are a debt security with equity-like features (in certain circumstances, like a share, they have no right to a return of capital). Although there are not any rights such as

<sup>46</sup> Muhd Ramadhan Fitri Ellias and colleagues, *Perpetual Sukuk: A preliminary shariah assessment*, 2015, p.2.

<sup>47</sup> As interest-bearing deposits are not permitted by the rules and principles of the Islamic Shari'ah, Islamic banks typically raise deposits in the form of profit-sharing investment accounts. These accounts differ from conventional deposits not merely by virtue of the profit-sharing nature of the returns they offer, but also because the contract between the depositors and the bank is not a debt contract and the deposits are in consequence not 'capital certain' (that is, the depositors are required to accept negative returns or losses). /Profit-sharing investment accounts in Islamic banks: Regulatory problems and possible solutions (PDF Download Available from: [https://www.researchgate.net/publication/247478992\\_Profit\\_sharing\\_investment\\_accounts\\_in\\_Islamic\\_banks\\_Regulatory\\_problems\\_and\\_possible\\_solutions](https://www.researchgate.net/publication/247478992_Profit_sharing_investment_accounts_in_Islamic_banks_Regulatory_problems_and_possible_solutions)).

this option for the issuer of Sukuk, but because of partial ownership of holder of asset-backed Sukuk in underlying asset, it is possible for that asset to be destroyed and the holder should bear the losses and has no right to a return of capital because holder has participated in a partnership and accepted profits and losses together so at least theoretically, they are not able to claim about that asset, anymore. As we can see, Sukuk (asset-backed one) can be like knock out bonds in some aspects. However, it is possible for issuer or originator of Sukuk to accept the losses through pre-agreement or insure the underlying asset and through this avoid the risks of Sukuk investor.

#### *3.3.3.4 Risks of Conventional Hybrids in Comparison with Sukuk*

Some key risks in related to hybrid securities are interest rate risk, credit risk and liquidity risk. Here we want to explain about insolvency risk and credit risk in Sukuk in comparison with mentioned securities. Each type of hybrid security has unique risk and reward characteristics. Convertible bonds offer greater potential for appreciation than regular bonds, but pay less interest than conventional bonds and still face the risk that the underlying company could perform poorly and fail to make coupon payments or not be able to repay the bond's face value at maturity. Convertible securities offer greater income potential than regular securities, but can still lose value if the underlying company underperforms. Other risks of hybrid securities include deferred interest payments, insolvency, market price volatility.<sup>48</sup> However we want to say that in asset-backed Sukuk the risk of insolvency and credit risk maybe not exist.

Actually, it is necessary to differentiate asset-backed and asset-based Sukuk, as their character is different in case of default. Asset-backed Sukuk is directly related to the underlying asset as guided by the Shariah principle; this Sukuk structure is therefore more in accord with Shariah principles, in which any risks related to and credibility of, the Sukuk are directly related to underlying assets. The risk or loss derived from underlying asset is subject to be borne by the Sukuk holder as a real owner of assets.<sup>49</sup> In line with ownership of underlying asset, Asset-backed Sukuk

<sup>48</sup> Read more: Hybrid Security

<http://www.investopedia.com/terms/h/hybridsecurity.asp#ixzz4fYu14xug>.

<sup>49</sup> Nazar, Jhordy Kashoogie, Regulatory and Financial Implication of Sukuk's Legal Challenges for Sustainable Sukuk Development in Islamic Capital Market, 8th international conference on Islamic economics and finance, center for Islamic economics and finance, Qatar faculty of Islamic studies, Qatar foundation, 2011, p.6.

holder has recourse towards underlying asset in case of default, which means that the Sukuk holder could take the underlying asset to cover their losses. Therefore, in an asset-backed structure, true sale should be executive.

Asset-based Sukuk, on the other hand, does not undertake true sale in the structure. This is more aligned with conventional bond structures. The Sukuk holder has a right that covers the underlying asset rather than ownership of the underlying asset itself; accordingly, they have recourse to the originator in case of default. In this regard, the investor's concern will differ depending on whether they are focused on the asset value itself or on the creditworthiness of obligor.<sup>50</sup>

In the process of issuance of asset-backed Sukuk based on underlying asset and in relation to the specific asset working as the basis for their issuance, Sukuk holders have objective and in fact priority right, comparing to other creditors; so, they would not be faced with bankruptcy risk. Of course, in case the same specific asset is lost, the loss will be imposed on Sukuk holders, as the owners of that asset. As for example in convertible bonds, performance of the issuing company affects price of security in the market; in terms of Sukuk also, reduction of price of underlying asset will affect price of Sukuk security in the market. In other words, holder of asset-backed Sukuk as the owner of the asset receives the value of the underlying asset based on current market price, on the due date; while, the value may have been reduced. It should be mentioned that, a solution has also been forecasted regarding the risk of reduction of underlying asset value; and, the risk will be eliminated with the help of insurance companies. Moreover, from credit risk point of view, in asset-backed Sukuk, the holders are considered as the owners of the asset and in case the issuer fails to make the payments, they may collect their rights from the asset; while, this is not the case with other securities including hybrids.

## 4 Conclusion

As observed, Sukuk are considered as Islamic securities which hold characteristics of both stocks and securities together, like other hybrid securities. Introduction of Sukuk and comparing them to common bonds and

<sup>50</sup> Tariqullah Khan and colleagues, *Legal and Regulatory Issues in Issuing Sukuk in Muslim-minority countries, Lessons from Developed Countries' Experience*, p.8.

company stocks were studied in different sections of the paper. At the end, we came to the result that Sukuk are a new type of hybrid securities; and, comparing some new models of Sukuk with various hybrid securities, we mentioned that “as hybrids consisting of various types such as convertible bonds, preference shares, subordinated bonds, perpetual bonds and knock-out bonds, Sukuk also are of various modern types in addition to their common and simple type, which could be cited as convertible, preference, subordinated and perpetual Sukuk.

As stated before, common bonds and hybrids bear such risks as credit risk of the issuer, bankruptcy risk of the issuer, value reduction of the issuer's company, all of which may affect the price of hybrid security. However, asset-backed Sukuk may be free from risks pertaining to bankruptcy of the issuer or his credit risk and may not be confronting the risk related to failure of the issuer in payment of asset-related revenue or profit, because of its specific nature which is a kind of ownership of underlying asset for issuance of Sukuk. The reason is that, in all of the above mentioned cases Sukuk holder may refer to the underlying asset to collect principal and also profit of the security and he has priority right in terms of underlying asset. This does not happen in relation to other hybrid securities, company stocks, or those bonds which are backed just through credit of the issuer. Considering global tendency towards usage of Sukuk in some countries such as England, Germany, Hong Kong, etc. it seems that more countries can use this instrument as a new and attractive type of hybrids. Certainly, the issue requires some specific regulations to be set for Sukuk, such as tax-related regulations in terms of securities, so that; these securities could be transacted with lower costs. Secondary markets for these securities also have to become prevalent, so that; liquidity problem would not be arisen, in respect of these types of securities.

## Appendix

Table of Distinguishing Sukuk from Conventional Bonds:<sup>51</sup>

| Categories                   | Conventional bonds   | Sukuk (asset- backed)   |
|------------------------------|--|---|
| Asset ownership              | bonds don't give the investor a share of ownership in the asset, project, business, or joint venture they support. They're a debt obligation from the issuer to the bond holder.                 | Sukuk give the investor partial ownership in the asset on which the Sukuk are based.  |
| Investment criteria          | Generally, bonds can be used to finance any asset, project, business, or joint venture that complies with local legislation.   | The asset on which Sukuk are based must be sharia-compliant.  |
| Issue unit                   | Each bond represents a share of debt.  | Each Sukuk represents a share of the underlying asset.  |
| Issue price                  | The face value of a bond price is based on the issuer's credit worthiness (including its rating).  | The face value of Sukuk is based on the market value of the underlying asset.   |
| Investment rewards and risks | Bond holders receive regularly scheduled (and often fixed rate) interest payments for the life of the bond and their principal is guaranteed to be returned at the bond's maturity date.         | Sukuk holders receive a share of profits from the underlying asset (and accept a share of any loss incurred).                             |
| Effects of costs             | Bond holders generally aren't affected by costs related to the asset, project, business, or joint venture they support. The performance of the underlying asset doesn't affect investor rewards. | Sukuk holders are affected by costs related to the underlying asset. Higher costs may translate to lower investor profits and vice versa. |

<sup>51</sup> How Sukuk (Islamic securities) Differ from Conventional Bonds, Available at: <http://www.dummies.com/personal-finance/islamic-finance/how-Sukuk-islamic-bonds-differ-from-conventional-bonds>.

## References

1. AAOIFI Shari'ah Standard (17) on investment Sukuk.
2. Abdul Karim Abdullah, Asset-backed vs asset-based Sukuk, Islamic finance-theory and practical use of Sukuk bonds, available at: [www.webcache.googleusercontent.com](http://www.webcache.googleusercontent.com)
3. Abdullah, Abdul Karim, Asset-backed vs asset-based Sukuk, 2012.
4. ACCA, Islamic finance – theory and practical use of Sukuk bonds, FEBRUARY 2013.
5. Afshar, Tahmoures A., USA compare and contrast Sukuk (Islamic securities) with conventional bonds, are they compatible?, School of business, Woodbury university, the journal of global business management volume 9, number 1, 2013.
6. Al-Bashir, Muhammad, Al-Amine, Muhammad, Sukuk Market: Innovations and Challenges, Islamic Economic Studies, Vol.15, No.2, 2008.
7. Ayotte, Kenneth M., Goan, Stav, Asset- backed securities: Costs and benefits of bankruptcy remoteness, 2010.
8. Barzel, Yoram, Economic analysis of property rights, Second edition, Cambridge cb21rp, United Kingdom, Cambridge University press.
9. Emir Hidayat, Sutan, A Comparative Analysis between Asset Based and Asset Backed Sukuk: Which One is More Shariah Compliant?, International SAMANM Journal of Finance and Accounting, July 2013, Vol. 1, No. 2.
10. Farooq, Mohammad Omar, Partnership, Equity-Financing and Islamic Finance: Whither Profit-Loss Sharing?, Review of Islamic Economics, Vol.11, special Issue,2007.
11. Godlewski, C, Turk-Ariss, R, & Weill, L., Sukuk vs. conventional bonds: A stock market perspective, Journal Of Comparative Economics, 41, 2013.
12. Hakim. S, Islamic money market instruments, in M. Hasan & M. Lewis, (eds), Handbook of Islamic Banking, Edward Elgar Publishing,2007.
13. Hesse, Heiko, Jobstandreas, Sole, Juan, Trends and challenges in Islamic finance, Word economics, Vol.9, No.2, 2008.

14. How Sukuk (Islamic securities) Differ from Conventional Bonds, available at: <http://www.dummies.com/personal-finance/islamic-finance/how-Sukuk-islamic-bonds-differ-from-conventional-bonds>
15. IIFM Newsletter, March 2017, Issue 1.
16. IIFM Sukuk Report (5th Edition), A Comprehensive study of the Global Sukuk Market.
17. Khnifer, Mohammad, When Sukuk default-asset priority of certificate-holders vis a vis creditors, University of Reading, ICMA Centre, Opalesque Islamic finance intelligence, No.11, 2012.
18. KonSik Kim, a civil law jurist's perspective on intermediary risk in the indirect holding system for securities: a comment on schwarcz& Benjamin, 2002.
19. Merritt, Cam, What Is the Meaning of Securitization? Available at: [www.homeguides.sfgate.com/meaning-securitization-6615.html](http://www.homeguides.sfgate.com/meaning-securitization-6615.html)
20. Muhd Ramadhan Fitri Ellias and colleagues, Perpetual Sukuk: A preliminary shariah assessment, 2015.
21. Nazar, Jhordy Kashoogie, Regulatory and Financial Implication of Sukuk's Legal Challenges for Sustainable Sukuk Development in Islamic Capital Market, 8th international conference on Islamic economics and finance, center for Islamic economics and finance, Qatar faculty of Islamic studies, Qatar foundation, 2011.
22. Norman, Trevor, Sukuk: Where next?, Newhorizon, 2009.
23. Pahlavan, Hamid; Razavi, Sayyed Ruhollah, "Sukuk (Islamic securities), definition, types and structure, management of Islamic researches and studies, Securities and Exchange Organization of Iran.
24. Securities Commission Malaysia (SCM), Sukuk, Sweet & Maxwell Asia, 2009.
25. Sukuk; Equity or Bonds? Available at <http://www.idealratings.com/Sukuk-equity-or-bonds.html>
26. Tariqullah Khan and colleagues, Legal and Regulatory Issues in Issuing Sukuk in Muslim-minority countries, Lessons from Developed Countries' Experience.
27. Taskhiri, Mohammad Ali, Sharia-defined foundations of Islamic securities(Sukuk), Islamic Economy quarterly, vol.7, No.27, 2007.



28. Understanding Hybrid Securities, available at:  
[www.asx.com.au/documents/products/Understanding\\_Hybrid\\_Securities.pdf](http://www.asx.com.au/documents/products/Understanding_Hybrid_Securities.pdf)
29. Vaez Barzani, Mohammad; Dallali Isfahani, Rahim; Aale Busuylam, Moslem, Engineering Islamic financing system, collection of articles, 2nd International Conference on Development of Financing System in Iran, 2010.
30. Visser, H., Islamic Finance: Principles and Practice, Gloucester: Edward Elgar.
31. What Is the Difference Between Asset-Backed Sukuk and Asset-Based Sukuk? Available at <http://investment-and-finance.net/islamic-finance/questions/what-is-the-difference-between-asset-backed-Sukuk-and-asset-based-Sukuk.html>

Webpages:

32. <http://www.dummies.com/personal-finance/islamic-finance/how-Sukuk-islamic-bonds-differ-from-conventional-bonds>
33. <http://www.dummies.com/personal-finance/islamic-finance/how-Sukuk-islamic-bonds-differ-from-conventional-bonds>
34. <http://www.investment-and-finance.net/islamic-finance/e/exchangeable-Sukuk.html>
35. <http://www.investment-and-finance.net/islamic-finance/s/senior-Sukuk.html>
36. <http://www.investopedia.com/terms/h/hybridsecurity.asp>
37. <http://www.investopedia.com/terms/h/hybridsecurity.asp#ixzz4fYu14xug>
38. <http://www.investopedia.com/terms/p/preference-shares.asp>
39. [https://www.researchgate.net/publication/247478992\\_Profit](https://www.researchgate.net/publication/247478992_Profit)
40. <https://www.Sukuk.com/article/Sukuk-taxation-legal-structures-2332/#sthash.F8waPFyg.dpuf>

