

## **EXPLANATORY NOTE ON ISSUANCE AND SUBSCRIPTION OF SUKUK IN LABUAN INTERNATIONAL BUSINESS AND FINANCIAL CENTRE**

### **1.0 Introduction**

- 1.1 As part of the efforts to facilitate and promote the development of the Islamic capital market, in particular the Islamic bond (sukuk) market in Labuan International Business and Financial Centre (IBFC), the Explanatory Note on Issuance and Subscription of Sukuk in Labuan IBFC has been introduced to clarify the requirements for the issuance and subscription of sukuk in Labuan IBFC.

### **2.0 Legal Provision for Sukuk Issuance in Labuan IBFC**

- 2.1 The issuance of sukuk in Labuan IBFC is subject to the provisions of Part III of the Labuan Islamic Financial Services and Securities Act 2010 (LIFSSA).

### **3.0 Eligible Issuers**

- 3.1 Any person<sup>1</sup>, through the establishment of a Labuan company or registration of a foreign Labuan company under the Labuan Companies Act 1990, may make an offer or invitation to subscribe for sukuk in or from Labuan IBFC.
- 3.2 An offer or invitation to subscribe for sukuk by a Labuan company or a foreign Labuan company to residents of Malaysia must be made through a Labuan Islamic bank licensee or a Labuan bank licensee (as the arranger for the offer of sukuk) unless otherwise allowed in writing by Labuan FSA.

---

<sup>1</sup> "Person" includes a corporation, partnership, a body of persons, corporate or unincorporated and a corporation sole.

## 4.0 Approval Requirements

- 4.1 Any person who makes an offer for subscription or purchase or issues an invitation to subscribe for or purchase sukuk (subsequently referred to as offer for subscription of sukuk) in or from Labuan IBFC, must obtain prior written approval from Labuan FSA under Section 13(1) of the LIFSSA, unless the offers or invitations of sukuk are excluded from the approval requirements of Labuan FSA as specified under Section 13(5) of the LIFSSA.
- 4.2 Section 13(5) of the LIFSSA stipulates that the following offers or invitations of sukuk are excluded from the requirement for prior written approval of Labuan FSA:
- For an offer or invitation of sukuk, where:
- (i) The first time investment of each of the initial sukuk holders is not less than two hundred and fifty thousand ringgit or the equivalent in any other currency and they are in possession of sufficient information to make a reasonable evaluation of the offer or invitation; or
  - (ii) The first time investment of each of the initial sukuk holders is less than two hundred and fifty thousand ringgit or the equivalent in any other currency and the number of persons to whom the offer or invitation is communicated does not exceed fifty and they are in possession of sufficient information to be able to make a reasonable evaluation of the offer or invitation.
- 4.3 For the issuance of sukuk that falls under Section 13(5) of LIFSSA, Labuan trust companies as the resident secretary of the Labuan company shall notify Labuan FSA not later than 30 calendar days after the issuance of the sukuk in Labuan IBFC.
- 4.4 A resident of Malaysia who makes an offer for subscription of sukuk in or from Labuan IBFC, is subject to the requirements of the Capital Markets and Services (Amendment) Act 2015 and the Foreign Exchange Administration Rules issued by Bank Negara Malaysia<sup>2</sup>.
- 4.5 A non-resident who makes an offer for subscription of sukuk in or from Labuan IBFC is required to register the disclosure document with the Securities Commission Malaysia as specified in the Capital Markets and Services (Amendment) Act 2015.

---

<sup>2</sup> Please refer to Notice 2 – Borrowing and Guarantee under Bank Negara Malaysia’s Foreign Exchange Administration Rules.

## **5.0 Eligible Investors**

- 5.1 Any person may subscribe to the sukuk issued in or from Labuan IBFC.
- 5.2 Residents of Malaysia may subscribe to the sukuk issued in or from Labuan IBFC, subject to the requirements under the Foreign Exchange Administration Rules issued by Bank Negara Malaysia<sup>3</sup>.

## **6.0 Shariah Adviser Requirement**

- 6.1 The endorsement of a Shariah adviser is required for the issuance of sukuk that falls under Section 13(1) of LIFSSA. The endorsement shall include a confirmation from the Shariah adviser that the documentation, structuring, investment as well as other administrative and operational matters in relation to the sukuk is in compliance with Shariah principles.

## **7.0 Appointment of Trustee and Agent**

- 7.1 A Labuan company which offers sukuk pursuant to Section 13(1) of LIFSSA shall make provision in the sukuk, or in a trust deed relating to the sukuk, for the appointment of a Labuan trust company as a trustee for the sukuk holders.
- 7.2 Labuan FSA may approve any other person to act as a trustee together with the Labuan trust company for the sukuk holders.
- 7.3 The offer or invitation of sukuk under Section 13(1) of the LIFSSA shall be made through an agent which shall be a Labuan trust company, an Islamic bank licensee or a Labuan bank licensee.

## **8.0 Governing Law**

- 8.1 The offering documents shall clearly state the applicable governing law. Notwithstanding this, for any sukuk issuance that falls under section 13(1) of LIFSSA, the relevant provisions of LIFSSA in relation to the issuance and subscription of sukuk shall apply, and are to be complied with at all times.

---

<sup>3</sup> Please refer to Notice 3 – Investment in Foreign Currency Asset under Bank Negara Malaysia’s Foreign Exchange Administration Rules.

## 9.0 Depository and Settlement

9.1 The foreign currency-denominated sukuk issued out of Labuan IBFC can be settled via International Central Securities Depositories such as Euroclear and Clearstream.

## 10.0 Listing of Sukuk

10.1 The foreign currency-denominated sukuk issued out of Labuan IBFC may be listed in any of the international exchanges including the Labuan International Financial Exchange (LFX).

## 11.0 Disclosure Requirements

11.1 For the disclosure requirements on the sukuk issuance, the sukuk issuer is encouraged to be guided by the IFSB-19 "Guiding Principles on Disclosure Requirements for Islamic Capital Market Products (Sukuk and Islamic Collective Investment Schemes)" where applicable.

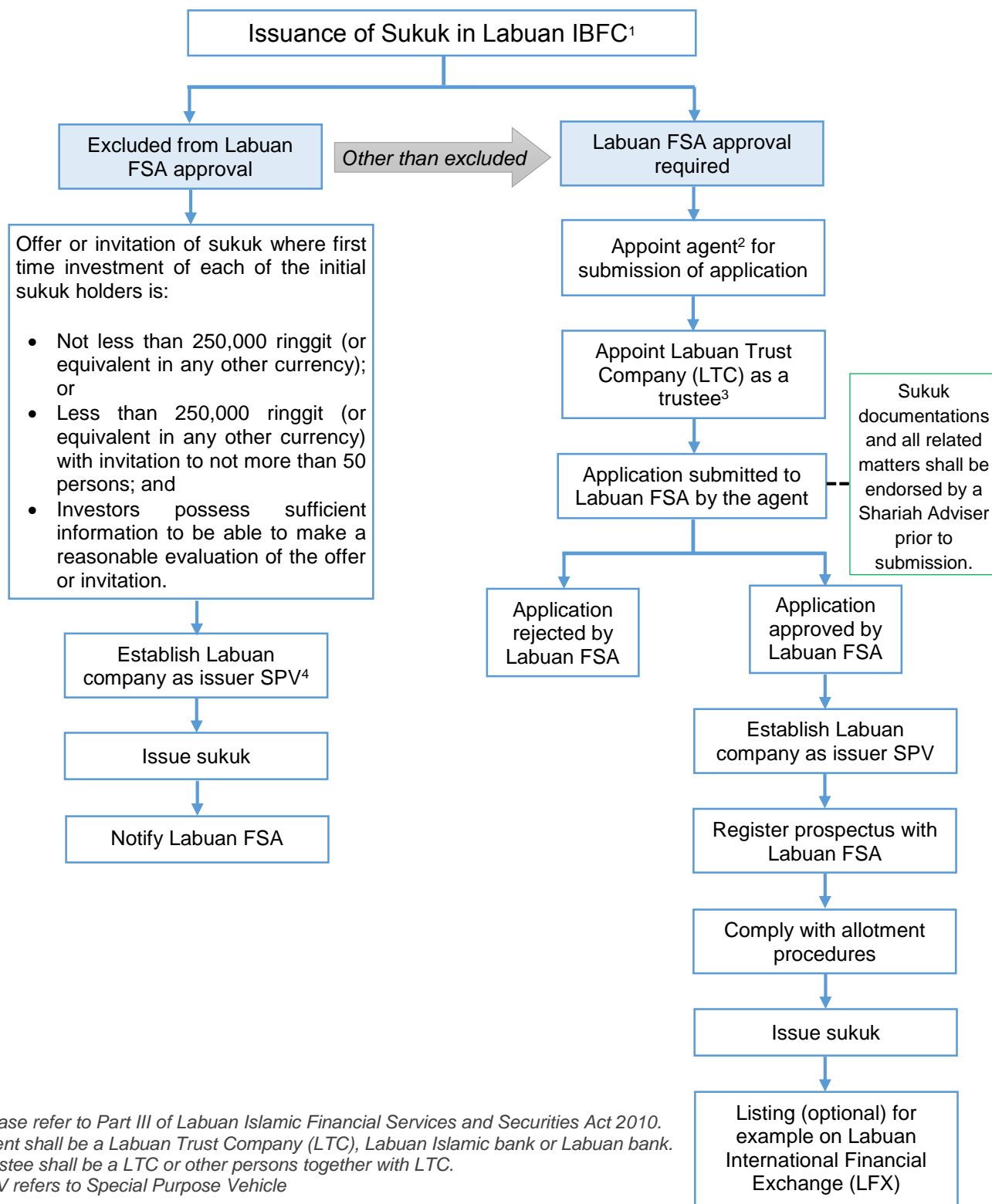
## 12.0 Reference

12.1 The flowchart on the issuance of sukuk in Labuan IBFC under Section 13(1) of LIFSSA is attached as Appendix I.

**Labuan Financial Services Authority**  
**24 October 2017**

**"Disclaimer:** This Explanatory Note is provided without any warranty, express or implied, as to its' legal effect and completeness. Take notice that any information provided herein is for informational and reference purposes only and does not constitute legal advice. Whilst the information contained herein has been formulated with all due care, it shall not in any circumstances be construed as constituting any legal obligation on the part of Labuan FSA. Independent professional advice should be sought where appropriate for further clarification. In no circumstances will Labuan FSA be liable or responsible for any damages or losses whatsoever, including without limitation, special, indirect or consequential arising out of or related to the reference, use or reliance of the information provided herein, whether by action, in contract or tort or otherwise howsoever."

**FLOWCHART ON ISSUANCE OF SUKUK IN LABUAN IBFC**



<sup>1</sup> Please refer to Part III of Labuan Islamic Financial Services and Securities Act 2010.  
<sup>2</sup> Agent shall be a Labuan Trust Company (LTC), Labuan Islamic bank or Labuan bank.  
<sup>3</sup> Trustee shall be a LTC or other persons together with LTC.  
<sup>4</sup> SPV refers to Special Purpose Vehicle

**FREQUENTLY-ASKED QUESTIONS  
EXPLANATORY NOTE ON ISSUANCE AND SUBSCRIPTION OF SUKUK IN  
LABUAN INTERNATIONAL BUSINESS AND FINANCIAL CENTRE**

**1. How are sukuk (Islamic bonds) different from conventional bonds?**

Sukuk is a trust certificate whereas a bond is a contractual debt obligation. Generally, sukuk represents a beneficial ownership interest in the underlying assets. Returns on sukuk are tied to the returns earned through the underlying assets.

For bonds, the issuer is contractually obliged to pay bond holders, the interest and principal on certain specified dates.

**2. What is the advantage of sukuk compared to conventional bonds?**

Sukuk have distinct advantages compared to conventional bonds:

Sukuk	Conventional Bonds
<ul style="list-style-type: none"> <li>✓ Sukuk is based on underlying transaction which creates a close link between financial and productive flows.</li> </ul> <p>The financing must be channelled for productive purposes, rather than speculative activities. This contributes to greater stability of the financial system.</p>	<ul style="list-style-type: none"> <li>✓ Conventional bonds is a debt obligation which separate risks from the underlying assets.</li> </ul> <p>This can lead to multiple layers of leveraging, increasing the potential for instability in the financial system.</p>
<ul style="list-style-type: none"> <li>✓ Sukuk issuance gives access to wider investor base as sukuk attracts both Islamic and conventional investors.</li> </ul>	<ul style="list-style-type: none"> <li>✓ The investor base for conventional bonds is confined to conventional investors.</li> </ul>
<ul style="list-style-type: none"> <li>✓ There is growing demand for sukuk arising from growing awareness on the universal values of Shariah in Islamic finance, increase in development and infrastructure projects as well as growing trend for ethical and socially responsible investing which are in line with the principles of Islamic finance and investment.</li> </ul>	

---

### **3. Why should I choose Labuan IBFC to issue sukuk?**

In taking a pro-business approach to its policies, Labuan IBFC complements Malaysia in offering a conducive environment for sukuk issuance with the following benefits:

#### Well-developed Islamic Finance Infrastructure:

- ✓ Comprehensive legal, regulatory and Shariah framework to ensure certainty and integrity in Islamic financial transactions.
- ✓ Breadth and depth of the Islamic capital market with wide range of Islamic financial instruments as well as diversified and skilled financial service providers.
- ✓ Pool of talent in structuring new innovative Islamic financial instruments.
- ✓ Wide investor base from Islamic and conventional financial institutions, pension funds and fund management companies.

#### Supportive Islamic Finance Ecosystem:

- ✓ Tax neutrality on all Islamic financial instruments and transactions.
- ✓ Stamp duty exemption on sukuk documentation.
- ✓ Liberal foreign exchange administration policy – free to use proceeds in and out of the country.
- ✓ Mutual recognition of Shariah opinions issued in other jurisdictions.

#### Strategic Location:

- ✓ Labuan IBFC is the gateway to Asia Pacific markets and economic opportunities, making it well placed for attracting investors for sukuk issuance.
- ✓ Competitive pricing, which may be better as compared to conventional bond pricing due to the high demand of sukuk in the region.

### **4. Who can issue sukuk in or from Labuan IBFC?**

Residents of Malaysia and non-residents can issue sukuk in or from Labuan IBFC. In addition, the issuance of sukuk by a resident of Malaysia is subject to the requirements of the Capital Markets and Services (Amendment) Act 2015 and the Foreign Exchange Administration Rules issued by Bank Negara Malaysia.

A non-resident who issues sukuk in or from Labuan IBFC is required to register the disclosure document with the Securities Commission Malaysia as specified in the Capital Markets and Services (Amendment) Act 2015.

**5. Can a non-Islamic company issue a sukuk?**

Yes. Any institution or company can issue sukuk as long as it is issued pursuant to the Shariah principles and concepts approved by the Shariah adviser appointed by the issuer.

Some prominent non-Islamic international companies that have issued sukuk include Nestle, International Finance Corporation (IFC, World Bank), the International Finance Facility for Immunization, Goldman Sachs Group, Toyota, Tesco and AEON Credit, a Japanese-based company.

**6. Who can purchase the sukuk issued in or from Labuan IBFC?**

Residents of Malaysia and non-residents can purchase the sukuk issued in or from Labuan IBFC. The subscription of sukuk by a resident of Malaysia is subject to the requirements under the Foreign Exchange Administration Rules issued by Bank Negara Malaysia.

**7. How do I make an informed investment decision as a sukuk investor?**

It is the responsibility of the investor to read and understand the prospectus before making a decision to invest. The prospectus is an important document which contains all the salient information on the sukuk issued, including the Principal Terms and Conditions and risk factors related to the issuance. Therefore, it is in the investor's interest to ask for a copy of the prospectus.

**8. What are the Labuan structures that can be used for the Special Purpose Vehicle (SPV) set-up to issue sukuk?**

The SPV shall be established in the form of a Labuan company structure or through the registration of a foreign Labuan company.

**9. What is the requirement for the trustee of the SPV established to issue sukuk?**

For sukuk issuance where the first time investment of each of the initial sukuk holders is less than RM250,000 (or equivalent in any other currency) and the invitation for subscription is to more than 50 persons, the Labuan company (SPV) shall appoint a Labuan trust company as the trustee for the sukuk holders.

Labuan FSA may approve any other person to act as a trustee together (co-trustee) with the Labuan trust company for the sukuk holders.



## 10. What are the fees payable for the Labuan SPV established to issue the sukuk?

The fees payable by the Labuan company SPV are illustrated in the table below:

Registration Fees	Amount	
<u>Paid-up Capital:</u>		
a) RM50,000 and below	RM1,000	USD300
b) Exceed RM50,000 but less than RM1 million	RM2,000	USD600
c) RM1 million and above	RM5,000	USD1,500
Registration of foreign company	RM6,000	USD2,000
Annual Fees	Amount	
Labuan company	RM2,600	USD800
Foreign Labuan company	RM5,300	USD1,500

## 11. What are the types of sukuk structures that can be issued in or from Labuan IBFC?

Among the sukuk structures that can be issued are Sukuk al-Ijara, Sukuk al-Mudaraba, Sukuk al-Musharaka, Sukuk al-Murabaha, Sukuk Wakala Bil-Istithmar as well as other sukuk and hybrid sukuk structures that are approved by the Shariah adviser.

The sample of sukuk structures based on the Shariah principles of Ijarah, Murabaha, Musharaka and Mudaraba are provided in the appendix A, B, C and D, respectively.

## 12. What are the types of underlying assets that can be used to structure sukuk in Labuan IBFC?

Examples of the underlying assets that can be used include real estate, factories, building, equipment, vehicles, rights to services, Ijara assets, sukuk certificates, Shariah-compliant shares, istisna' receivables, Murabaha receivables and any other assets approved by the Shariah adviser as underlying assets for the sukuk issuance.

### **13. Why should I list my company's sukuk?**

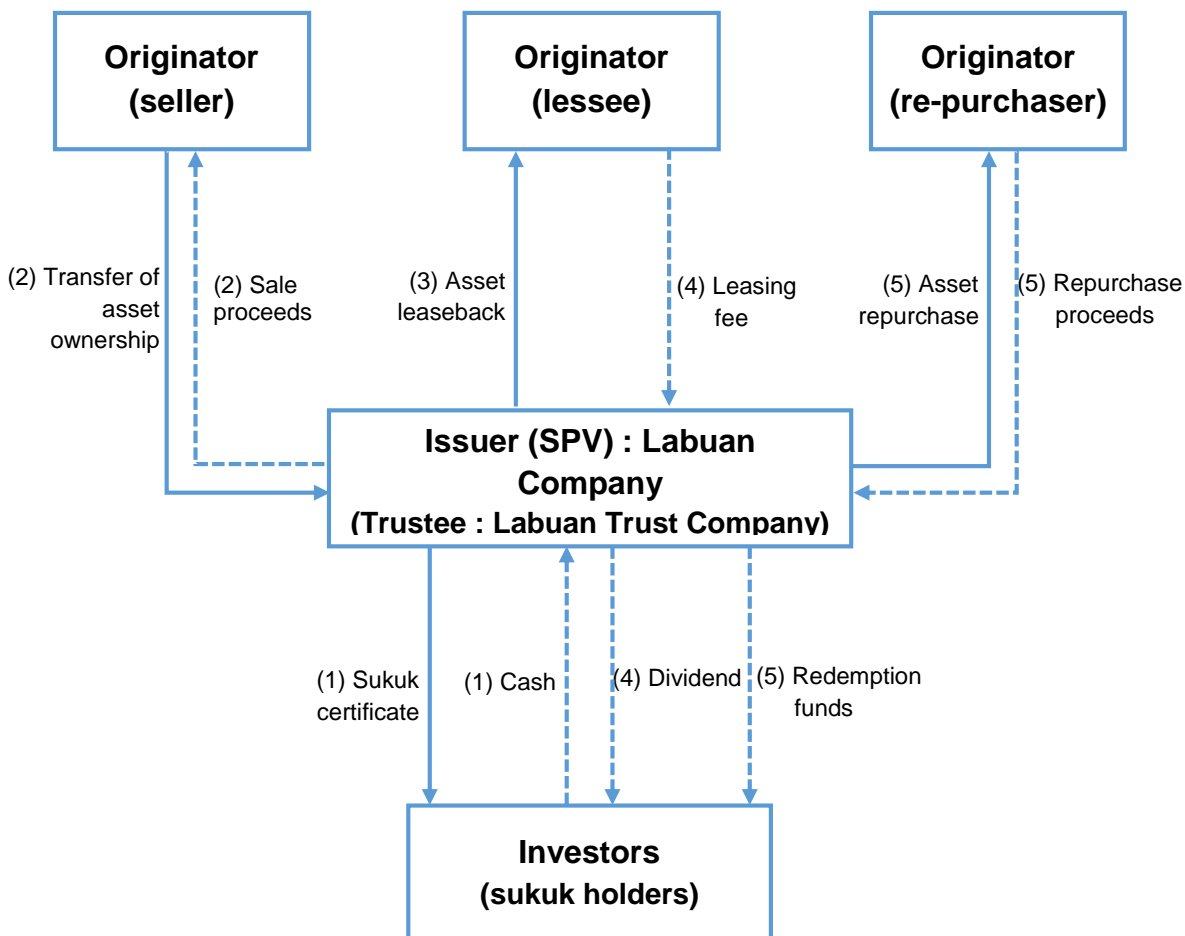
The sukuk issued out of Labuan IBFC may be listed in any of the international exchanges including the Labuan International Financial Exchange (LFX). The listing of sukuk in international exchanges such as LFX provides the following benefits to the issuer:

- ✓ Unique exposure and access to diverse international and regional investors to enhance marketability and tradability.
- ✓ Provides for investor confidence as it ensures greater transparency, discipline, accountability and efficiency.
- ✓ Enhance profile of the issuer among investors.
- ✓ Provides secure, stable and flexible financing for the issuer's needs at a competitive cost of capital.
- ✓ Creates a market for sukuk, providing opportunity to increase liquidity and enhance their attractiveness to investors.

### **14. What are the governing legislations involved in issuing or offering sukuk in Labuan IBFC?**

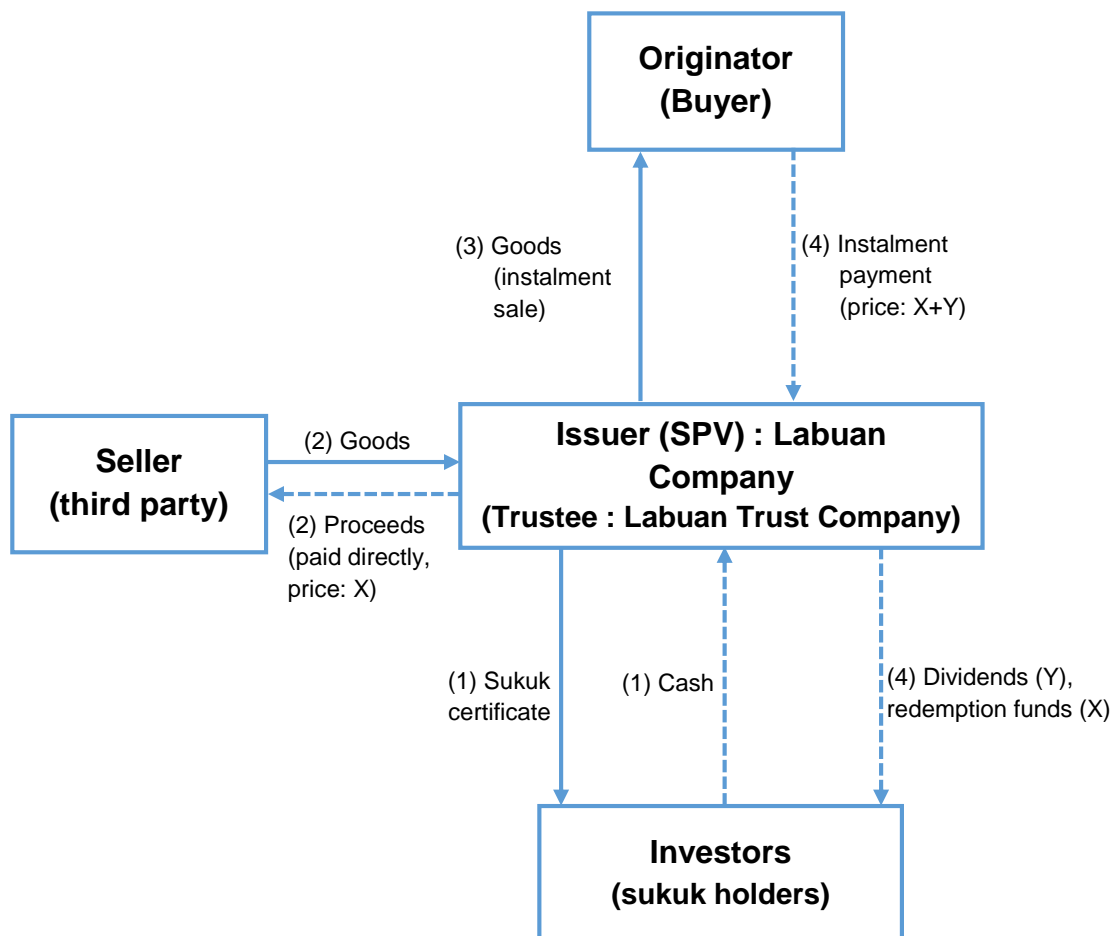
The establishment of a Labuan company or registration of foreign Labuan company is governed by the Labuan Companies Act 1990.

In addition, for the issuance of sukuk, the governing law is the Labuan Islamic Financial Services and Securities Act 2010 (Please refer to Part III of the Act).

**SAMPLE OF IJARAH SUKUK STRUCTURE**

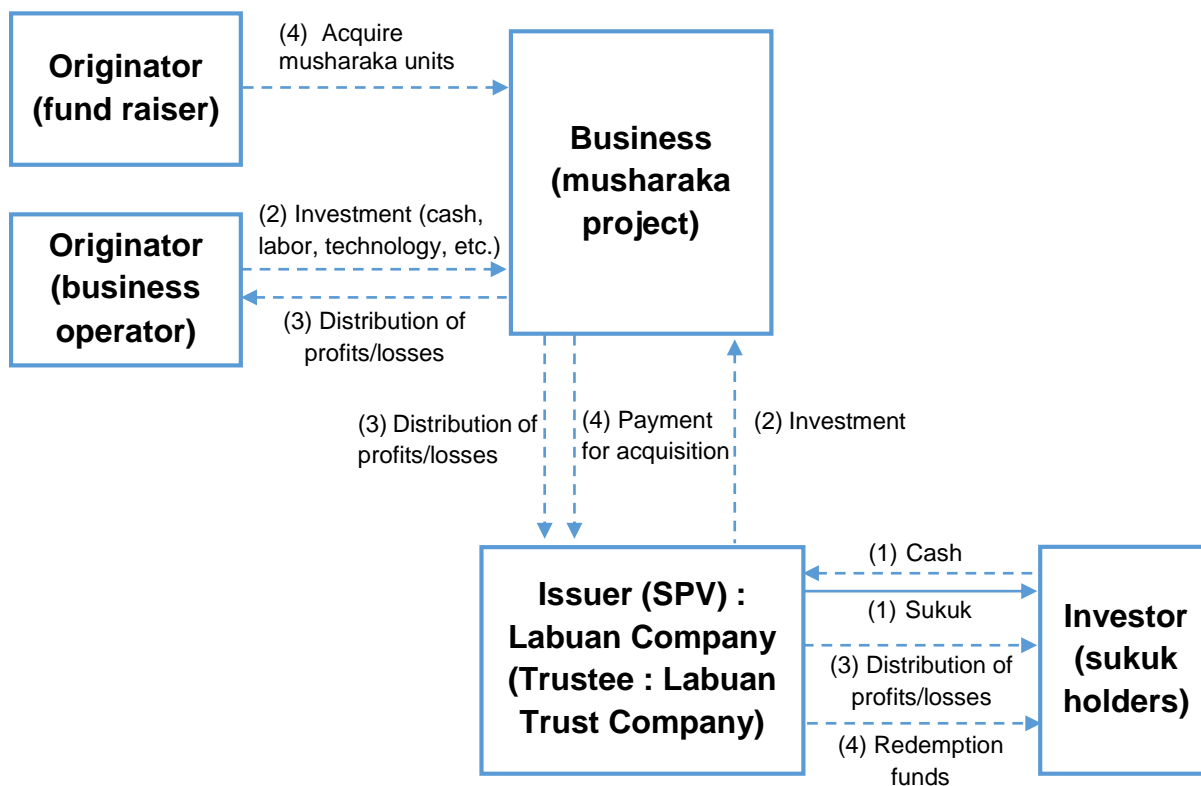
*Note: The dotted-line arrows indicate cash flow.*

1. The originator establishes a Labuan SPV and issues sukuk to raise funds.
2. Acting as a trustee for the investors, the SPV uses the collected funds to purchase the underlying assets, paying to the originator the purchase price, which is the same as the amount of sukuk issuance.
3. The said assets are leased back to the originator based on the initially signed ijarah contract.
4. The leasing fee generated by the assets is the source of funds for the dividends paid to the sukuk holders via the SPV.
5. The originator repurchases the underlying assets when the sukuk matures and the proceeds are used for redemption.

**SAMPLE OF MURABAHA SUKUK STRUCTURE**

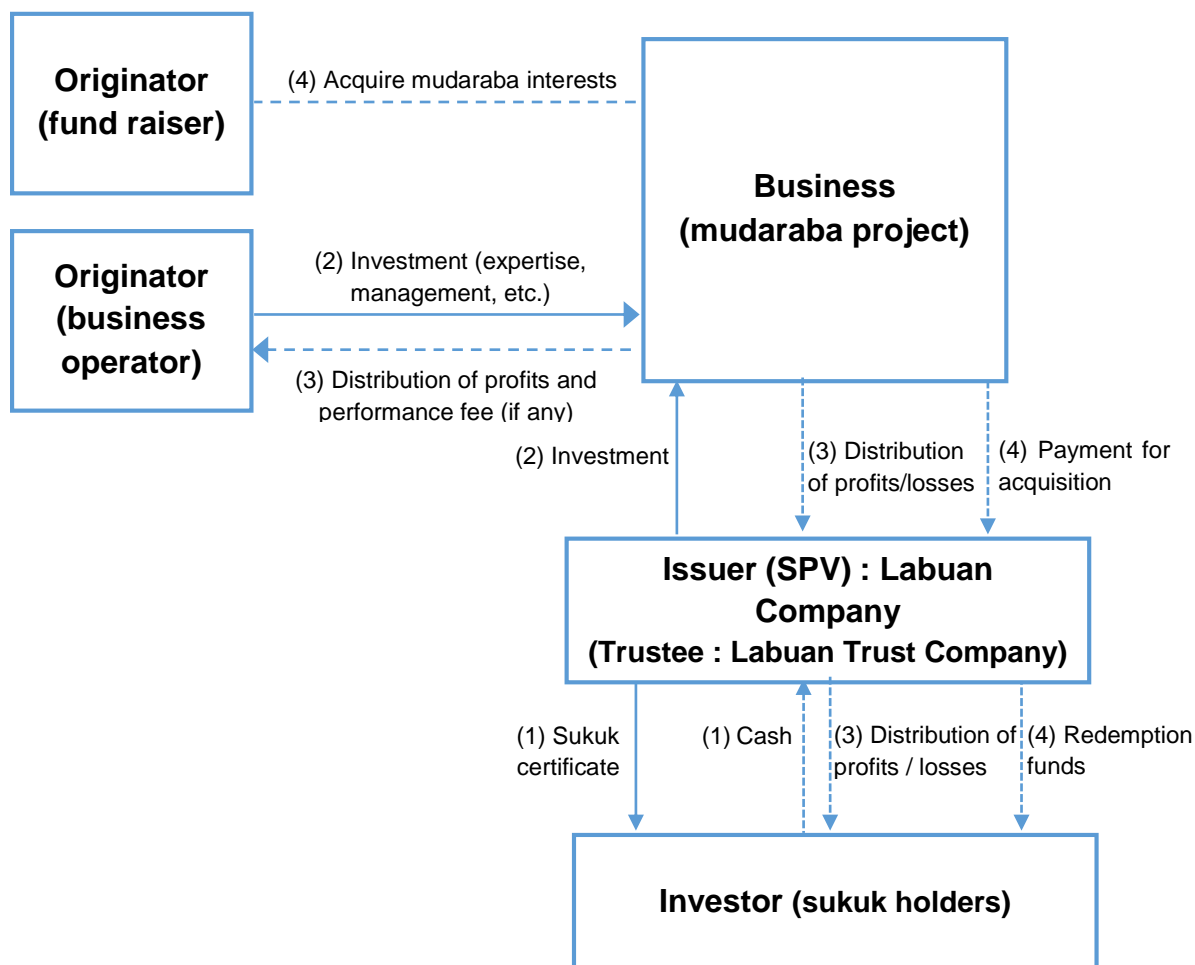
*Note: The dotted-line arrows indicate cash flow.*

1. The originator establishes a Labuan SPV and issues sukuk to raise funds.
2. Acting as a trustee for the investor, the SPV uses the collected funds to purchase the goods requested by the originator.
3. The SPV then resells the purchased goods to the originator at a mark-up price and on an instalment basis.
4. The instalment payment from the sale will be paid to the investors and are used to fund redemption.

**SAMPLE OF MUSHARAKA SUKUK STRUCTURE**

*Note: The dotted-line arrows indicate cash flow.*

1. The originator establishes a Labuan SPV and issues sukuk to raise funds.
2. The SPV, acting as trustee for the investor, enters into a musharaka contract with the originator, and invests the collected funds into the project.
3. The profits/losses generated by the project are shared with the sukuk holders.
4. When the sukuk matures, the originator acquires the musharaka business, and the proceeds are used to fund redemption.

**SAMPLE OF MUDARABA SUKUK STRUCTURE**

Note: The dotted-line arrows indicate cash flow.

1. The originator establishes a Labuan SPV and issues sukuk to raise funds.
2. Acting as a trustee for the investor, the SPV uses the collected funds and enters into a mudaraba contract with the originator, and invests the collected funds into the project.
3. The profits generated by the project are shared between the originator and the sukuk holders. Any losses of the mudaraba project would be borne by the sukuk holders.
4. When the sukuk matures, the originator acquires the mudaraba business, and the proceeds are used to fund redemption.