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## **SHARIAH ISSUES OF OWNERSHIP AND POSSESSION OF ASSET-BASED *SUKUK* STRUCTURE: A SHARIAH SCHOLARS' PERSPECTIVE**

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### **ABSTRACT**

*Sukuk* serves as an instrument in the global Islamic financial market, which has experienced expansion in recent years. Despite this notable growth, *Sukuk* encounters Shariah-related concerns pertaining to the possession of underlying assets. This study investigates the Shariah perspective on *Sukuk* investors without full ownership or possession of the underlying asset under asset-based *Sukuk*. This study adopted a qualitative method and used primary and secondary data sources. Primary data was gathered from eight participants through semi-structured interviews with Shariah experts in Malaysia and Nigeria. NVivo 10 was used to analyse the data thematically. This study used relevant resources such as respected journals, textbooks, newspapers, and other relevant sources for secondary data. Our findings show that the *Sukuk* holders must take possession of underlying assets during

the duration of the project. Therefore, it is illegal for a person to sell assets that he or she does not own. A complete ownership transfer must occur, allowing *Sukuk* investors to lease the asset back to the government or issuer. The findings also reveal that the legal system of the country where the *Sukuk* was issued is one of the factors that restricts investors from receiving the underlying asset of *Sukuk*, particularly in asset-based *Sukuk*. The study's consequences include that the stakeholder's issue is *Sukuk* under Shariah legislation, attracting investors to participate in Shariah-compliant investments. Moreover, it is recommended that investors use underlying assets during *Sukuk* projects to avoid *gharar*.

**Keywords:** *Sukuk*, possession, asset-based, legal system, Shariah-compliance.

## INTRODUCTION

*Sukuk* stands out as one of the Islamic financial products that has experienced rapid and unparalleled growth across various countries over the past decade (Paltrinier et al., 2019; Raza & Ashraf, 2019; Nasr et al., 2016). In Shariah-compliant finance, *Sukuk* is an alternative to traditional bonds (Godlewski et al., 2016), and has gained practical acceptance in both Muslim and non-Muslim nations (Paltrinieri et al., 2019). According to Bello et al. (2018), *Sukuk* became a new phenomenon in the international financial market after the global meltdown. It is an alternative method of raising funds to address the financial crises of governments and firms and improve economic expansion and sustainability. Muborakbekovich (2021) stressed the importance of the *Sukuk* market because it attracts potential investors from government and corporate entities to invest in the *Sukuk* business.

Smaoui and Nechi (2017) mentioned that *Sukuk* allows private and public entities to diversify their financing needs and expand their capital pool to fund new projects and achieve sustainable growth. Biancone and Radwan (2018) identified *Sukuk* as an effective approach for financing large-scale projects, a method that was historically challenging for financial institutions or individual investors to implement. Financial institutions and Islamic banks can manage their liquidity by investing in *Sukuk*, which allows them to acquire *Sukuk* when they have excess liquidity and sell it on the secondary

market when it lacks liquidity. Similarly, Smaoui and Nechi (2017) showed that *Sukuk* growth energises financial inclusion and impacts economic growth positively.

With the rapid expansion of Islamic finance products, particularly *Sukuk*, many Western countries have recently allowed Islamic financial operations (Ghezal et al., 2022). For example, the United Kingdom is the hub of the Islamic finance capital of the West. *Sukuk* is similar to a government bond used to raise funds instead of traditional bonds (Djafri et al., 2021). Meanwhile, the German government established the first full-fledged Islamic bank in 2017 (Bhavin & Saad, 2017). In addition, the Japanese government has issued a directive that allows Islamic banking products to operate in the country (Djafri et al., 2021).

From 2010 to the third quarter of 2017, the most significant estimation of *Sukuk* issued was reported in 2012. In addition, the third quarter of 2017- 2013 saw the most significant number of *Sukuk* issuances. However, the market saw a decrease in *Sukuk* issuance in 2016 concerning value and quantity. This phenomenon has been ascribed to the diminished oil prices and the allure of conventional bonds (Al-Ali, 2019). The global *Sukuk* market distribution in 2017 indicated that Asian countries accounted for 72.1 percent of global *Sukuk* issuance, followed by the GCC (23.3%), European countries (2.36%), and African countries (2.2%). On the other hand, countries that contributed to the universal *Sukuk* market were Malaysia as the leading country with a total share market of 62.4 percent, followed by the United Arab Emirates (UAE, 7.3%), Saudi Arabia (9.7%), Indonesia (6.4%), Bahrain (2.8%), Qatar (2.6%), and Türkiye (2%) (IIFM, 2018; Al Asari, 2018).

Furthermore, from 2001 to 2017, Malaysia played a dominant role as the biggest *Sukuk* issuer in both international and domestic markets, with USD 612 billion, followed by Saudi Arabia (\$95 billion), the UAE (with an unlimited amount of \$95 billion), and Indonesia (\$63 billion). The universal *Sukuk* percentage of 68.9 percent belonged to Malaysia and Indonesia, as Malaysia accounts for 62.5 percent and 6.4 percent of Indonesia (COMCEC, 2018; Paltrinieri et al., 2019; IIFM, 2018). This shows that the UAE has 27.01 percent, thus maintaining leadership in the global *Sukuk* market. Malaysia follows this (25.77%) and Saudi Arabia (19.67%) (IIFM, 2021).

However, with this development, the *Sukuk* is bedvilled by Shariah's challenges and legal issues of possession in *Sukuk* structures. There are debates among Islamic scholars on *Sukuk* offered in many markets (Benaicha et al., 2019; Utami et al., 2019). Significant challenges have emerged relating to Shariah's compliance with the *Sukuk* (Hosen, 2016; Safian, 2017; AbdulKareem et al., 2022). The investors' ownership and possession of the underlying asset were questionable. By definition, 'possession' or 'ownership' refers to an asset's physical or constructive acquisition and ownership. The transfer of ownership involves the physical conveyance of the item from the seller to the buyer, while the transfer of possession encompasses a symbolic conveyance of the asset through tamkin, enabling the buyer to assume possession, along with other mechanisms aimed at removing impediments that could hinder the purchaser from taking control 'Possession' refers to acquiring Shariah-compliant *Sukuk*, either constructively or physically, on the Islamic capital market (ICM) (Yosoualhi, 2017; Ghezal et al., 2022).

There have been questions about whether all *Sukuk* holders have possessed or owned completely the underlying asset of the *Sukuk* before selling it in the ICM. Asset-based *Sukuk* is an example of this, in which the underlying asset of the *Sukuk* does not leave the originator's balance sheet after being purchased by *Sukuk* investors. This led to arguments over Shariah's compliance with asset-based *Sukuk* that is not owned or possessed by investors. Most Shariah scholars have ruled out that the asset-based *Sukuk* structure is not Shariah-compliant because investors should possess the underlying assets. As an unresolved issue among Shariah scholars and practitioners, this deviation from Shariah has raised the critical question of how *Sukuk* investors, with full ownership or possession, will follow the provisions of Shariah compliance with the contract. Hence, this study intends to investigate the Shariah viewpoint of *Sukuk* investors without full ownership or possession of the underlying asset of *Sukuk* under asset-based *Sukuk* based on Islamic jurisprudent evaluation. This issue is related to the country's legal system, where the *Sukuk* was issued.

## LITERATURE REVIEW

*Sukuk* is defined by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) as '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 activity' (AAOIFI, 2010, p. 298). Furthermore, it is similarly defined as 'certificates of equal value put to use as common shares and rights of intangible assets, usufructs, and services or as equity in a project or investment activity' and this definition is supported by many researchers (Ahmed & Elsayed, 2018; Olaide & AbdulKareem, 2021; Smaoui & Khawaja, 2017; Godlewski et al., 2016; Asutay & Hakim, 2017; Mahmud et al., 2019). *Sukuk* investors are interested in the underlying asset of *Sukuk*, a project, an enterprise business, which enables them to receive incomes generated from the projects (Hasan et al., 2019). In Islamic finance, the *Sukuk* is the most important financial instrument. Western investors perceive *Sukuk* as a debt-like fixed-income instrument; conversely, Muslim investors opt for *Sukuk* due to its adherence to Islamic principles, aligning with their financial requirements, in contrast to conventional bonds *Sukuk* can also meet the needs of investors who want to diversify their equity holdings with low-risk bonds. *Sukuk* is a more cost-effective business borrowing option than syndicated loans (Radzi, 2018; Rafay et al., 2017). It can aid in expansion, mergers, procurement, and international operations (Rafay et al., 2017).

The rapid growth of *Sukuk* issuance is fuelled by several factors, such as the increased recognition of *Sukuk* instruments by universal financial experts, the increase in Islamic investment liquidity (IIL) searching for *Sukuk*, increase in retail and corporate interest in Islamic finance, and the increased standardisation of unsecured Islamic structures. In general, the *Sukuk* industry's development factors remain stable. Universal growth of *Sukuk* increased slightly from 3.4 percent in 2014 to 3.5 percent in 2015, owing to lower expansion, supportive cash-related conditions, and continuous universal exchange growth (Barghouthi et al., 2020). Furthermore, S&P Global (2022) mentioned that they "expected stronger *Sukuk* issuances and further expanded market shares during the modest recovery of core Islamic finance economies to boost Islamic finance assets by around 10 percent to 12 percent over 2021 to 2022." *Sukuk* is a Shariah compliance instrument that compliments the traditional bonds, which contain two main differences. There are three prerequisites for *Sukuk* to be considered a Shariah compliance instrument: (1) the *Sukuk* certificate must represent ownership of intangible assets, usufructs, or services from income-generating projects; (2) payments to *Sukuk* investors

come from projects after tax; and (3) the repayment of an asset value at maturity date should follow the current market price of the *Sukuk* asset and not the first invested amount. *Sukuk* has various strictures, and financiers are not limited to creating their varieties. However, the primary parties in *Sukuk* issuance are the originator, SPV, and investors purchasing *Sukuk* certificates (Zolfaghari, 2017; Rajapakse & Senarath, 2019).

The functions of *Sukuk* have evolved, and a fundamental description of the current *Sukuk* is that it serves as a financial instrument enabling key stakeholders to raise substantial funds from investors. This can be accomplished by constructing a new *Sukuk* structure with underlying assets. Lenders and borrowers are involved in the traditional bond process, whereas *Sukuk* investors and issuers are involved through Islamic contracts. To issue a *Sukuk*, issuers must secure assets. *Sukuk* investors who are interested in buying or subscribing to a *Sukuk* investment will receive a certificate as proof of asset ownership. *Sukuk* investors are eligible to receive money that is equal to the value of the underlying asset of the *Sukuk* upon maturity. The *Sukuk*'s asset value can fluctuate depending on the value of the underlying asset. These characteristics distinguish *Sukuk* from bonds (Razak et al., 2019).

Based on commercial and technical *Sukuk* features, Hasan et al. (2019) classified *Sukuk* into asset-backed and asset-based structures. The underlying asset of the *Sukuk* structure remains on the originator's balance sheet after the issuance of asset-based *Sukuk*. The originator owns the asset, and the asset's beneficial ownership is given to the *Sukuk* holder, while the issuer retains legal ownership. According to Ahmed et al. (2019) and Hosen (2016), the asset-based *Sukuk* structure does not reflect an actual asset sale. This is because such *Sukuk* holders do not own the underlying asset. This equally makes the *Sukuk* holder have no legal right to sell the asset to a third party other than the originator of the *Sukuk* asset. Sulaiman (2020) stated that *Sukuk* holders under the asset-based *Sukuk* have full ownership or possession of underlying assets that do not belong to investors. Naifar and Hammoudeh's (2016) asset-based *Sukuk* structure incorporates tangible assets that might not be legitimately admitted to being possessed or entirely owned by the *Sukuk* investor. This *Sukuk* structure awards only beneficial ownership to the investors of *Sukuk* and indicates that investors of *Sukuk* do not have full recourse to the *Sukuk* assets of the *Sukuk* project, which are not utilised as collateral.

On the other hand, an asset-backed *Sukuk* structure is the transfer of the underlying asset of the *Sukuk* from the originator to the *Sukuk* investors, who are paid from the income generated by the underlying asset of a *Sukuk* project (Nada et al., 2016). Investors in asset-backed *Sukuk* can sue the issuer if the issuer defaults. Furthermore, the underlying asset has been transferred from the originator's balance sheet to the investors' (Tasniaa et al., 2017; Nada et al., 2016). According to Senarath Rajapakse and Rajapakse (2019b), in an asset-backed *Sukuk*, the obligor transfers legal ownership of the underlying asset to a third party, usually a Special Purpose Vehicle (SPV). The SPV acts as a trustee for the *Sukuk* holder, issuing a *Sukuk* certificate and collecting a fee from the holders. *Sukuk* holders are the legal owners of asset projects, and any proceeds from *Sukuk* investments based on project performance go to the holders. Similarly, a *Sukuk* asset has been transferred from the originator's balance sheet to the *Sukuk* holders' balance sheet. Indeed, in the event of default, the *Sukuk* investor, as the legal owner, has the exclusive right to sell the *Sukuk* to recoup the money without going through the obligor (Ahmed et al., 2019). As a consequence, the most critical distinction between asset-backed and asset-based financing lies in the treatment of the asset in the event of default.

Shariah's Position of *Sukuk* Holders without Owning or Possessing an Underlying Asset. First, the issue to be discussed is selling what someone does not own. To validate any selling contract in Islam, the object matter must be exited and owned by the seller. Selling an asset unowned or possessed by the seller is a form of *gharar* (uncertainty), as guided by hadiths. In addition, such a transaction where the asset is not owned or possessed by the seller could lead to a Shariah issue, namely beneficial ownership in asset-based *Sukuk*, which could trigger a problem in case the issuer defaults and *Sukuk* holders have not possessed or owned the underlying asset of *Sukuk* (Nada et al., 2016). Some hadiths mentioned the prohibition of reselling the asset before taking possession (Rahman, 2020). *Qabd* implies receipt or possession of something so that the new buyer can carry out the contractual disposition of the asset without any hindrance (Alam et al., 2017). An asset possession gives the *Sukuk* investor the authority to lease the asset back to the originator. However, unfortunately, under the asset-based *Sukuk*, an underlying asset is not possessed or owned by the investors.

Aziz and Ahmad (2018) viewed the qabd as everything that leads to ownership of goods and permits the use of commodities, which is based on the common local practices without having to hold the commodity on the hands or hold legal ownership. ISRA (2018) defines qabd as the possession of a specific asset, either constructively or physically. Regarding the possession status in a sale contract, Hanafi scholars do not view possession as an essential sale requirement, but as a subsidiary condition instead (Majallah Section 262). It is legally permissible to defer it to a later date, with the exception being transactions involving ribawi items, where qabd is essential as a prerequisite for a valid contract. The Malik scholars confined the application of the hadith on possession to food grains, implying that some other class of items, such as palm oil and cotton, may be sold before collection. Ibn Umar cited Prophet Muhammad (PBUH) as saying, “Whoever buys food, he should not resell it before he takes possession of it” (Sunan Abu Dawud; Rahman, 2020; AAOIFI, 2010).

Additionally, there is no argument among Muslim scholars that possession of ribawi food items (e.g., wheat, dates, notably, salt, and barley) is a condition for their sale. Concerning non-ribawi food, on the other hand, the Maliki scholars have two opinions: (1) it is prohibited without prior possession, and (2) it can be sold without prior possession (Guelida et al., 2022). From the Shafi’e scholars’ perspective, possession is the primary condition for property types. They strictly adhere to the literal meaning of a hadith mentioned as quoted, “Do not sell anything until you receive it,” to the degree that even selling out immovable objects must fulfil the possession prerequisite before resale (AAOIFI, 2010). In any case, the perspective of the Shafi’e school is not applied by the other schools, which do not compel possession before a resale in the event immovable objects such as land. Most Islamic scholars’ jurisprudence holds that the reason for disallowing sales before taking possession is mainly due to the presence of gharar, which may lead to misunderstanding among the transacting parties. This resulted from the worry that the goods may not be delivered because of damage or other issues. Along this line, Islam prohibits any transactions, including bay al ma’dum, as the delivery of the subject matter cannot be performed and may cause gharar (Rahman, 2020).

The purchaser must subsequently take ownership of the underlying asset, and it is also necessary to evaluate the underlying asset’s liability for loss and damage. The risk connected with the underlying asset is



the buyer's responsibility, as long as the asset is under his control (Uddin & Ahmad, 2020). Offers and acceptances can be transmitted verbally or by other means that elicit the contracting parties' approval. Apart from security and registration, this agreement does not need to be written and documented; however, Shariah recommends keeping a record of the contract (Ribadu & Rahman, 2019; AbdulKareem et al., 2023). As owners of the underlying asset, *Sukuk* holders must be able to trade with the *Sukuk* asset freely. This establishes the concept of ownership and possession from a Shariah perspective, which states that *Sukuk* holders must have unrestricted access to the underlying asset. In contrast, the *Sukuk* holder has no legal right to sell the underlying assets, especially in the event of default. This condition sparks a discussion among Shariah scholars about whether the *Sukuk* holder receives ownership of the *Sukuk* or if the relationship between the *Sukuk* holder and the originator is simply like a creditor and a debtor (Uddin et al., 2015).

There are two categories of ownership based on the Shariah principle: (1) complete ownership and (2) incomplete ownership. Complete ownership entails unrestricted rights to legally dispose of them if the asset still exists. In addition, it is impossible to eliminate an asset's ownership right, as it may render the property ownerless (Alaro, 2017; Ghani, 2017).

Ownership, according to Al-Zuhayli (2003, p. 1126), is an exclusive association of the owned thing with its owner, giving the owner the freedom to deal with what he owns in any way that is not legally barred. When a property is legally acquired, the proprietor holds the exclusive right to use and manage it, provided there are no legal impediments to their operations. This right is not applicable to children and individuals with mental health issues, as they do not possess such rights.

This condition prohibits others from exploiting the property without legal permission, such as a guardianship agency (Ghani, 2018). Furthermore, from an Islamic perspective, Hammad (2008, p. 2) defined ownership as a legal claim by a person over an item, to the degree that he is free to transact with it and restrict others from interacting with it. It was also mentioned that ownership and other rights must be established appropriately. More importantly, these rights are based on Islamic law. Legal rights are assigned to the property's vicegerent, who uses the property according to Islamic beliefs (Abdul Razak & Saupi, 2017).

According to Lahsasna et al. (2018), the underlying asset ownership must be transferred and registered in the name of the *Sukuk* holder, not just written to enjoy the asset benefit. When a payment is completed, the issuer issues a certificate, which serves as proof of ownership of the underlying asset. *Sukuk* holders have the right to claim their investments even if they go bankrupt. However, if the investment is damaged, only the *Sukuk* holder will take the loss in proportion to the percentage of the asset they own to justify the profit earned from the *Sukuk* investment. The existing literature demonstrated that scholars had diverse opinions on these phenomena, up to the point that some scholars stated that most *Sukuk* structures did not comply with Shariah. Future studies can further investigate these issues in advanced countries in the *Sukuk* market, Malaysia in particular, and provide some lessons for other countries practicing *Sukuk*, especially Nigeria, and how to make Nigeria lead in Islamic finance, particularly *Sukuk* in the African region.

## METHODOLOGY

The main objective of this study is to investigate Shariah scholars' viewpoints of *Sukuk* investors about not having full ownership or possession of the underlying asset under asset-based *Sukuk* based on Islamic jurisprudent evaluation. To accomplish the study's objective, a series of in-depth interviews was conducted with Shariah scholars in Malaysia and Nigeria. The research employed a qualitative approach that incorporated both primary and secondary data. Researchers use three types of interviews in the qualitative approach: unstructured, semi-structured, and structured, which can be conducted online, over the phone, or in person (Arsel, 2017; Schober, 2018). Several research methodologies are called triangulation, which harmonises the aim for which another may reward one.

Various data collection methodologies and triangulation-assisted data analysis were conducted to meet the research objective. In social research, semi-structured interviews are the most extensively used method for gaining an in-depth understanding of social occurrences (Dzwigol, 2020; Alam, 2021). A list of questions was created for respondents regarding the issues under the specified investigation. Furthermore, this strategy elicits information from interviewees about their own experiences and understanding of the topic (Saunders et al., 2016). On the other hand, a semi-structured interview technique

might provide a more in-depth perspective or information based on pre-arranged questions about diverse situations (Knight et al., 2018).

Purposive sampling was used to select the study participants. Although the sample size was small, it is considered normal under the qualitative approach because the participants were chosen based on criteria identified as significant in addressing the phenomenon (Creswell & Poth, 2018). A few aspects considered in selecting the participants of this study were their experience and education related to the phenomenon. These participants hold different positions in Islamic jurisprudence (*fiqh*), and some were Shariah supervisory members of other countries. Before performing the analysis, verbatim transcription was performed for the interviewees. In addition, the NVivo 10 programmes were used to speed up the coding, sorting, and storage of transcripts for analysis. In-depth interviews with eight people were conducted. Based on a guide by Kegler et al. (2019), the participants were coded according to their country of origin to ensure data confidentiality. Participants from Malaysia were referred to as SSMs, while those from Nigeria were referred to as SSNs.

Malaysia and Nigeria were chosen as case studies; both countries have common law jurisdiction. Moreover, Malaysia is considered mature in the Islamic finance industry in terms of the management by the government in the issues of legal and beneficial ownership in *Sukuk* structures without contradiction with Islamic law. Nigeria, as an infant in Islamic finance (*Sukuk*), can learn from Malaysia's experiences. Similarly, Malaysia and Nigeria do not need to enact provisions that allow legal ownership based on the common law in each country, permitting the transfer of only beneficial ownership of assets. Shariah scholars were chosen because of their experience and education related to Islamic finance, particularly in *Sukuk*. These Shariah scholars held different positions in Islamic jurisprudence, and of them were Shariah supervisory members of different countries.

## **FINDINGS AND DISCUSSIONS**

### **Status of Possession**

The participants shared a wealth of knowledge about Shariah issues related to asset-based *Sukuk* arrangements, including ownership and possession. As mentioned previously, Shariah scholars have

differing views on whether *Sukuk* holders must completely control the underlying asset in asset-based *Sukuk*. Most participants, however, agreed that *Sukuk* holders must own the underlying asset before leasing it back to the issuer. As one of the participants (SSN 3) emphasised:

*“In every Sukuk structure, owners must fully possess the assets during the project’s tenure. There must be a transfer of full ownership that will give the Sukuk holders the right to lease the asset back to the government or the issuer. The issuer will pay rent to SPV as a trustee on behalf of the investors, which will be resold back to the issuer on maturity or any triggered event. However, if Sukuk owners do not have the right to the assets, the contract is not Shariah-compliant. Regarding absolute ownership of Sukuk assets, the holders must be eligible to own the asset. When it comes to total ownership, investors must own something. The prophet (PBUH) says, ‘You cannot sell what you do not own’ and therefore, the Sukuk holders must own assets before they can be sold back to the issuer.”*

In the same view, participant SSN 1 supported the claim:

*“According to Shariah, ownership and possession are the best means of claiming profit or dividing it from what an investor owns. Shariah ownership qualifies investors to earn dividends or profits. Similarly, there is no issue if investors earn profit or dividends in asset-based Sukuk. A parameter can be used to determine whether investors possess or own the asset. For instance: (1) It has to look at who bears the brunt in any event of loss, whether the Sukuk holders or the originator. If it is structured so that someone claims the profit but is not liable for the loss, In that case, this is different from the kind of ownership recognized by Shariah to qualify an investor to earn a profit. (2) Another parameter to determine who is entitled to the underlying asset If an asset is sold today, who is entitled to the proceeds? This parameter can be used to determine whether Sukuk holders own assets as Shariah requires.”*

In line with this discussion, Ghani et al. (2021) posited that Islamic regulation emphasises the ownership of assets. This means that the possession of an asset guarantees its utility by the owner's. In corroborating this, Rahman (2020) and Lahsasna et al. (2018) affirmed that all transactions must comply with Shariah rules and regulations. This implies immediate possession of the assets after the contract is concluded. The *Sukuk* holder must possess the asset before being hired back by the *Sukuk* issuer.

Furthermore, participant SSM 3 bolstered other participants' arguments on the issue of possession of underlying assets of asset-based *Sukuk* by stating:

*“Full possession of assets is a requirement in Shariah. When referring to underlying assets, the Sukuk owner does not fully possess the asset. First, it must differentiate between possession and the rights of Sukuk holders. No matter the type of Sukuk, be it ijarah, musharakah, or mudarabah, there must be a sale of the underlying asset and a transfer of ownership. Shariah recognises the transfer of ownership, in which there must not be a restriction for Sukuk holders regarding the underlying assets. The current practice in the market is that in some transactions, the issuer places certain restrictions on the property, and the Sukuk holder needs proper due diligence regarding the asset. This restriction or condition should be removed to ensure that the investors have ownership and possession of the asset, whether registered under the investors' names or not.”*

From the previous discussion, one can assert that ownership and possession are crucial aspects of asset-based *Sukuk* structures. The right to possession or ownership provides the *Sukuk* holder with the authority to dispose of the underlying asset to the *Sukuk* issuer or a third party. Therefore, the *Sukuk* holder should possess the underlying asset before renting it to the issuer (Lahsasna et al., 2018). The claims by Lahsasna et al. (2018) and AbdulKareem et al. (2023), further supported by participant SSN 2, are as quoted:

*“The issue of ownership and possession of the asset from the issuer to the Sukuk holders is another concern in the Sukuk structure in the case of default. There are different*

*interpretations of the AAOIFI and SAC of Malaysia. The AAOIFI stipulates that there must be a specific transfer of ownership from the issuer to the Sukuk holders and possession of the asset. For instance, in the East Cameroon Sukuk case, there was a disagreement between the issuer and the Sukuk holders that the underlying asset needed to be correctly transferred to the Sukuk holders after some years. It is not full possession transfer of ownership. This type of anti-crisis terminology in the AAOIFI standard opined that there must be a specific transfer of full ownership of the asset, unlike the SAC of Malaysia, which allows the transfer of ownership in some assets that belong to the government.”*

This situation gave such investors the right to claim the underlying asset back in case of default by the issuer; similarly, it afforded gharar in the contract. Conclusively, it is agreed from the interviews of the study that any *Sukuk* structure shall be as follows:

1. To ensure Shariah compliance with *Sukuk* transactions, investors should own and possess underlying assets;
2. To avoid gharar in the case of default, investors should own and possess the underlying assets;
3. To investigate *Sukuk* structures efficiently and effectively to prevent any possible non-Shariah compliance; and
4. Shariah scholars are the backbone of Islamic finance by providing a better and clearer *fatwa* before issuing the *Sukuk*.

### **Impact of the Legal System**

The importance of ownership and possession in *Sukuk* structures has been established. Similarly, Guelida et al. (2022) found the significance of ownership in any Islamic finance product as the authors focused on *waqf*. However, the participants discovered another aspect that has hampered *Sukuk* owners' ability to hold or possess the underlying assets of the *Sukuk* in several jurisdictions. They stated that one of the obstacles preventing investors from owning the underlying assets of *Sukuk* is the legal system of the country where the *Sukuk* is issued, particularly in the common law jurisdiction system. The legal system was crucial in preventing *Sukuk* holders from obtaining complete possession or ownership of the asset. Participants in SSM 4 stressed

that, as quoted, “there is no problem or harm regarding *Sukuk*. If the asset does not belong to the investors because, at inception, they are informed that the asset belongs to the government. The asset belongs to the public if the investors agree with the issuer; everything has been put up front. Therefore, this is a limitation of the public asset, as the investors have no possession but have the right to lease the asset back to the issuer. The fact is that this is public property, and only some structures have this issue. It is only a specific structure involving government assets that involves the public interest.”

In line with the abovementioned opinions, the legal structure under which *Sukuks* are created is a barrier to *Sukuk* investors’ complete possession and ownership of the project’s underlying asset. SSM 2 remarked, as quoted, “*Sukuk* investors do not possess the underlying asset. It usually happens in sovereign *Sukuk*, where the underlying asset belongs to the country. For example, in an airport or ministry building, all of these assets are generally not allowed to go to other parties. However, within *Sukuk*’s tenure, all the rights and liabilities of these assets belong to the investors. Investors do not have the right to sell these assets to a third party. Only the government has the right to repurchase it from investors.”

According to the IFSB (2009), the control of the underlying asset of *Sukuk* is contingent on the legal system under which *Sukuk* is issued. In addition, the right of investors to have *Sukuk* assets does not compulsorily include the registered title. Ownership possession could be a simple collection of ownership attributes that permit the *Sukuk* holder to step into the originator’s shoes or perform responsibilities related to ownership, in addition to the view that the legal system is an obstacle for some investors to have full possession or ownership of the underlying asset (AbdulKareem et al., 2023). According to SSM 2, as quoted, “It is the owner’s right to have ownership and possession of the asset as stated by Shariah, but the government limits the transfer of ownership. Based on the government regulation on the property, because it is very strategic, this issue is interrelated with government policy and the *masalah* of the country. All these must be considered when the *Sukuk* structure is peculiar to countries with a common law system.”

Another participant also supported the view that it depends on the country’s law, whether common law or civil law, where the *Sukuk* is issued. SSN 3 added, as quoted, “to have possession of the underlying

asset of *Sukuk* or full ownership of the *Sukuk* asset. It depends on the law of the country where *Sukuk* was issued, either common law or civil law. This is to be clarified under which law the *Sukuk* is structured. For instance, in Malaysia, legal ownership is not transferred in the case of reserved land. Therefore, if the *Sukuk* is structured based on this land, the *Sukuk* investors will not have legal ownership. Sometimes, Shariah law needs to be revised for contracts with certain assets. Hence, a country's custom can be applied if it does not contradict Shariah's principle. Therefore, purchasing *Sukuk* based on common law is not prohibited."

In addition, SSM 1 emphasised that the legal system in which *Sukuk* has been issued plays a critical role in any *Sukuk* structure, as quoted: "This is not a concern because investors have recourse to the underlying asset if *Sukuk* holders are legally recognised as owners. In addition, investors have liability on the asset under the condition of claimed profit, as indicated by Shariah. Hence, there is no restriction on them doing whatever they want. This proves that investors own the asset. If the originator defaults on paying investors monthly and quarterly payments and the ownership of the asset is still with the originator, the court will recognise the beneficiary of the investment even if the registration is under the originator; since the court recognises beneficial ownership, there is no big problem."

According to Alaro (2016) and AbdulKareem et al. (2023), English law divides ownership into beneficial and legal categories. This posed a new issue for Shariah experts regarding the legality of the underlying asset of *Sukuk*. This is corroborated by SSN 3's view, as quoted: "For me, there is no problem as far as the legal system of the country where *Sukuk* are issued recognised beneficial ownership without having a legal owner and possession of the asset, so there is no problem." In support of this view, SSM 5 also asserted that "*Sukuk* owners not having full possession of the underlying asset but whose rights are preserved and maintained have no serious issue. It is not necessary to register the asset under the name of the *Sukuk* holders; the name can be registered under the trustee as beneficial ownership."

However, in asset-based *Sukuk* structures, legal ownership of the asset does not belong to the *Sukuk* investors, similar to the legal system of common law in some jurisdictions, such as Malaysia and Nigeria. In the realm of the common law system, a clear distinction is drawn between



legal and beneficial ownership. Conversely, in jurisdictions governed by civil law, the delineation between legal and beneficial ownership is not a point of contention. In these civil law contexts, it is plausible that the nuanced issue of ownership and possession concerning asset-based Sukuk structures may not arise. This underscores the divergent legal frameworks and potential implications for Sukuk arrangements in different jurisdictions.

In a nutshell, the study's findings revealed that the legal system of the country where the *Sukuk* was issued played an essential part in ensuring that *Sukuk* owners were able to obtain control of the underlying asset. As a result, we may conclude that:

1. There are issues of lack of absolute ownership or full possession of government assets that are available to the public.
2. This occurs based on the *Moslah* of the country.
3. To maintain Shariah compliance with the contract, investors should assume the liability of assets for the contract period, and
4. This issue occurs in the *Sukuk ijarah* only because investors must take equity-based *Sukuk* ownership based on their contribution to the *Sukuk* projects.

The *Sukuk* issuer must critically observe Shariah requirements in every *Sukuk* structure, particularly the issue of possession and ownership of the underlying assets of *Sukuk*, so that it will not lead to non-Shariah compliance, such as issuing *gharar* in the underlying asset. Modern Islamic finance transactions prioritise ownership structures that comply with Shariah principles, which often involve shared ownership, asset-backed financing, and partnerships. These arrangements ensure that possession and ownership are aligned with Islamic values, thereby avoiding interest-based transactions and excessive uncertainty while promoting economic fairness and ethical conduct.

### **DANA GAS AS A CASE STUDY OF BENEFICIAL OWNERSHIP IN *SUKUK* STRUCTURES**

In asset-based *Sukuk* structures, beneficial ownership and possession are crucial in Islamic finance, particularly *Sukuk*. An actual case study

demonstrates this structure very well, which is known as the Dana Gas *Sukuk* dispute case in 2017. Dana Gas, an energy company based in the UAE, raised USD 920 million by issuing a *Sukuk* in 2007. This *Sukuk* was set up as a *mudarabah* certificate, a typical *Sukuk* structure in which investors contribute capital and the issuer manages the funds while sharing profits and losses.

In 2017, Dana Gas declared that according to the most recent interpretations of Islamic finance rules, the 2007 *Sukuk* was no longer Shariah-compliant. They claimed to restructure the *Sukuk* on more advantageous terms for the company because the *Sukuk* had become illegal due to modifications made to Islamic finance standards. According to Dana Gas, the *mudarabah* structure failed to give the *Sukuk* holders actual beneficial ownership and possession of the underlying assets of *Sukuk*. Investors in a *mudarabah* should partake in the actual profits and losses of the underlying assets under Islamic financial principles. The *Sukuk* structure, however, included clauses that fixed the returns, making it to look like a conventional bond. This led to concerns regarding the validity of *Sukuk* holders' ownership rights in the underlying assets. The *Sukuk* holders, on the other hand, asserted that Dana Gas's attempt to restructure the *Sukuk* amounted to a breach of contract and a contravention of Shariah rules because they were, in fact, the beneficial owners of the underlying assets. They thought that Dana Gas was trying to back out of its commitments and lower the payouts to *Sukuk* holders.

Eventually, the lawsuit was heard in courts in several countries, including the United Kingdom and the UAE. The results of this case greatly impacted the *Sukuk* market and the Islamic finance industry. In the end, a settlement was achieved in which Dana Gas consented to honour its original *Sukuk* obligations and pay a greater profit rate to the *Sukuk* holders. The Dana Gas *Sukuk* case study highlights the significance of beneficial ownership and possession in asset-based *Sukuk* structures. Transparency in *Sukuk* contracts must ensure that investors truly possess beneficial ownership and possession of the underlying assets, as required by Islamic finance principles. This case study underscores the paramount importance of aligning Islamic financial products with Shariah principles, emphasizing the need to maintain investor confidence and uphold market integrity. Additionally, it sheds light on the challenges and intricacies associated with navigating issues of possession and beneficial ownership within

asset-based *Sukuk* structures. The exploration of these complexities offers valuable insights into the dynamic landscape of Islamic finance and its intersection with legal and Shariah considerations.

## SUMMARY AND CONCLUSION

This study examines the Shariah perspectives of *Sukuk* investors who still require complete ownership or possession of the underlying asset in asset-based *Sukuks*. The findings showed that *Sukuk* holders must take possession of the underlying assets because it is illegal for someone to sell something they do not own. Furthermore, all *Sukuk* investors must fully acknowledge the underlying assets of the project's duration. A complete ownership transfer must occur, allowing *Sukuk* investors to lease the asset back to the government or issuer. The issuer will pay rent to the SPV as a trustee on behalf of the investors, who will then resell the bonds to the issuer at maturity or at any other time. *Sukuk* holders must own the asset before it may be sold back to the issuer, as quoted from the Prophet Muhammad (PBUH), "You do not sell what you do not own." According to Shariah, possession is the best way to claim profits from what one has, but investors cannot claim anything if they do not have possession, as Prophet Muhammad (PBUH) explained.

The findings also revealed that the legal system of the country where the *Sukuk* was issued is one of the reasons that prohibits investors from getting the underlying assets of the *Sukuk*, particularly in asset-based *Sukuk* structures. According to the participants' consensus, *Sukuk* can be sold from the originator to the *Sukuk* holders without the originator acquiring control of or holding the underlying asset of the *Sukuk*. The primary issue under Shariah is that investors can only benefit by bearing responsibility, yet because *Sukuk* holders benefit from the project, they must also take responsibility. Moreover, the purchaser must then take possession of the underlying asset and it is imperative to determine the liability of the underlying asset regarding the loss and damage. As long as the investors own the underlying asset, they are responsible for any risk (Uddin & Ahmad, 2020). Those who do not bear any responsibility are not qualified for compensation and income, as the Prophet disallowed the profit earned without taking risk and liability (Agha & Sabirzyanov, 2015; AbdulKareem et al., 2023).

One criticism of the current *Sukuk* structure is that the owner has yet to be transferred entirely or possessed by the *Sukuk* holder. As a result, it is critical to push the *Sukuk* issuer and the government to give *Sukuk* holders complete possession and ownership of the underlying asset over the project's duration. The stakeholder's influence would end non-Shariah compliance, which Shariah experts are fighting for. Similarly, to finally address the issue of possession and beneficial ownership in asset-based *Sukuk* structures in Malaysia and Nigeria, it is vital to strengthen regulatory oversight, enhance legal frameworks, and encourage awareness of Islamic finance principles among stakeholders. Additionally, IFIs should adopt Shariah-compliant and transparent possession and beneficial ownership in *Sukuk* structures to ensure the integrity of operations and transactions.

This research acknowledges certain limitations that warrant consideration. Primarily, the study faced constraints in reaching a broader spectrum of influential figures in the Islamic finance business within the given time frame. However, it is noteworthy that those few figures who were approached during this limited period displayed eagerness in sharing valuable insights, contributing significantly to the richness of knowledge and experience incorporated into the study. Secondly, a small sample size (eight participants) could only provide limited data and discussions. Finally, this research was focusing only on the Shariah issue of ownership and possession in asset-backed *Sukuk* arrangements. A valuable suggestion for future research involves employing a triangulation of quantitative and qualitative approaches to delve deeper into the issue, particularly in a different jurisdiction. This multifaceted methodology could offer a more comprehensive understanding and nuanced insights into the subject matter.

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