

SHARIAH GOVERNANCE and ASSURANCE in Islamic Financial Sectors

Islamic finance is commonly associated with *Shariah* governance and assurance. The current challenges and issues in the Islamic finance industry have mostly motivated the needs for a more comprehensive and robust *Shariah* governance and assurance. Thus, this book unearths contemporary issues pertaining to *Shariah* governance and assurance. The topics discussed in this book cover various issues in *Shariah* governance and assurance ranging in different sectors such as Islamic banking, Islamic capital market, Islamic social finance and other Islamic Muslim community in the effort to enhance the Islamic finance industry globally, particularly in Islamic banking, *takaful*, Islamic cooperative, Islamic social enterprise and Islamic non-profit organisations. Hence, this book is envisaged to elevate the knowledge of the society in Islamic finance especially on *Shariah* governance and assurance.



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FOREWORD

In the Name of Allah, Most Gracious, Most Merciful

السلام عليكم ورحمة الله وبركاته

Critical Readings in Shariah Governance and Assurance in Islamic Financial Sectors is an initiative by the PNB-USIM *Shariah Governance and Assurance Conference* (PNB-USIM SGAC 2017) team after successfully organizing the conference recently. All papers presented during the conference are compiled into a book that is suitable for all practitioners, academicians and other related parties who have interests in Islamic finance especially on *Shariah* governance and assurance.

This book provides readers with current knowledge on *Shariah* governance and assurance including Islamic banking, takaful, Islamic cooperative, Islamic social enterprise and Islamic non-profit organisation. I would like to take this opportunity to congratulate all editors and authors for their perseverance and persistent effort in completing this book.

Besides, I also would like to congratulate the Faculty of Economics and Muamalat (FEM) for winning the *Most Outstanding Islamic Finance Education and Research* award at the Kuala Lumpur Islamic Finance Forum (KLIFF 2017). This award was granted for the tremendous effort and endless support from all FEM members since the faculty's inception in 2001. Hopefully, this award will not stop our journey in strengthening the Islamic finance industry in Malaysia and world over.

This book contains essential readings that cover the topic of *Shariah* governance, *Shariah* assurance, *Shariah* disclosure and *Shariah* management perspectives. Therefore, it is hoped that this book will aid readers in understanding current Islamic finance industry practices, especially in *Shariah* governance and assurance as it provides comprehensive knowledge in the related area. Happy reading.

ASSOC. PROF. DR. MUHAMMAD RIDHWAN AB. AZIZ

Dean

Faculty of Economics and Muamalat

Universiti Sains Islam Malaysia

PREFACE

In the Name of Allah, Most Gracious, Most Merciful

السلام عليكم ورحمة الله وبركاته

All praise to Allah SWT and peace be upon to our beloved Prophet Muhammad SAW. Alhamdulillah, it is with His mercy and His blessings that we are able to publish this book entitled *Critical Readings in Shariah Governance and Assurance in Islamic Financial Sectors*.

This book is a compilation of papers/articles presented in the PNB-USIM *Shariah* Governance and Assurance Conference (PNB-USIM SGAC 2017) held in Kuala Lumpur. The conference was jointly organized by the Faculty of Economics and Muamalat (FEM), Universiti Sains Islam Malaysia (USIM) and Permodalan Nasional Berhad (PNB). This book covers various issues in *Shariah* governance, *Shariah* assurance, *Shariah* disclosure, *Shariah* management as well as Islamic accounting and reporting.

These contemporary issues are important to the Muslim banking and business community in enhancing their knowledge in the Islamic finance industry including Islamic banking, *takaful*, Islamic cooperatives, Islamic social enterprises and Islamic non-profit organisations. The content will be useful to the practitioners, professionals and regulators in understanding the current state of art of *Shariah* governance and assurance as practiced in the Islamic banking and finance industry, not only in Malaysia but also in other Muslim countries.

The Faculty of Economics and Muamalat, USIM has also initiated a training program, known as the *Shariah* Audit Training (SAT) that is conducted at an Islamic bank and an Islamic financial institution in 2016 and 2017, respectively. The training program consisting of eight modules which include *Shariah* principles, *Shariah* governance and assurance, *Shariah* audit process and programs have been successfully conducted in Islamic Financial Institutions (IFIs). The program, being the first of its kind in Malaysia, has also been accredited by the Financial Accreditation Agency (FAA), an agency under the Bank Negara Malaysia (BNM). This conference is an extension of the training program.

CONTEMPORARY STRUCTURING OF CORPORATE *WAQF* VIA ISLAMIC REAL ESTATE INVESTMENT TRUSTS (I-REITS): IS IT VIABLE?

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INTRODUCTION

Waqf or Islamic endowment is an important institution in the social sector (*ijtima'i sector*) of the Islamic economic system that has contributed significantly towards socio-economic and social development since the early days of Islam. There is an abundance of historical evidence that has shown the commendable contribution of *waqf* as a primary socio-economic vehicle for financing Muslim society (Hodgson, 1974) without incurring any cost to the government (Mohsin, 2010; Cizakca, 1998). A substantial amount of literature has discussed the great contributions of *waqf*, and the importance of effective and efficient management role of *waqf* institution in enhancing the socio-economic development.

Traditional *waqf* management, which relies solely on the honesty and trustworthiness of the *waqf* managers (*mutawallis*) in managing *waqf* properties, has been scrutinised due to the vulnerability of the system to corruption and mismanagement (Magda 2016; Shatzmiller, 2011; Magda, 2009). According to Dato' Seri Jamil Khir Baharom, Minister at the Prime Minister's Department of Malaysia, there are 11,000 hectares of *waqf* land worth of RM1 billion that has yet to be developed in Malaysia. This situation is one of the issues highlighted pertaining to the problems occurring in the administration

of *waqf* in Malaysia. In this case, this issues may highlight the issue of inefficiency and possibly unsystematic administration of different *waqf* management system within the different states of Malaysia. Therefore, recently, the government has called for a reform of the *waqf* management system in this country for the purpose of ensuring that all *waqf* assets are self-sustained and self-reliant from third parties to ensure sustainable growth and continuous return to beneficiaries.

The concept of corporate *waqf* has emerged as one of the solutions whereby a pool of *waqf* assets will be managed by professional managers. Corporate *waqf*, which combines recurring charity with entrepreneurial dynamism power, has emerged as a new avenue in the administration of modern *waqf* in the quest of finding ways to accelerate *waqf* development in Malaysia through governance and management best practice. The fast growing Islamic finance industry has necessitated the emergence of modern financial instruments that comply to *Shariah*, such as *sukuk*, Islamic real estate investment trusts (I-REITs) and Islamic unit trusts. These financial instruments are rigorously regulated by the Securities Commission of Malaysia with the purpose of promoting good governance to ensure the sustainability and resilience of the capital market. On that note, this study aims to understand and explore the potential of an Islamic capital instrument, namely the Islamic real estate investment trust (I-REITs) as an avenue to address the issue of unattended and undeveloped *waqf* assets in Malaysia. To achieve this objective, the application of Islamic REIT in developing *waqf* assets is proposed.

LITERATURE REVIEW

The Concept of *Waqf*

According to Ibn Qudamah, *waqf* is “withholding the original (property) and distributing the yields (outcome)” (Ibn Qudamah, 1985). The prevailing characteristic of *waqf* is perpetuity by retaining the assets (with an implied ownership of belonging to God, hence non-disposable) and to devote its utilisation for the benefit of mankind. The salient features of perpetuity and repetitive flow of income or services produced by *waqf* assets are clear manifestations that *waqf* assets should not be left idle. This is important to ensure sustainable returns for the beneficiaries. This is evidenced by the fact that most

of *waqf* assets during the Prophet PBUH's time generated continuous benefits for Muslims such as the construction of Nabawi Mosque as well as the famous Khaybar land and the Ruma well which were endowed as *waqf* by Umar al-Khattab and Uthman ibn Affan respectively. Essentially, *waqf* is *sadaqah jariyyah* (running charity) which is different from normal *sadaqah* (giving). The *sadaqah jariyyah* concept implies a Muslim's willingness to sacrifice his belongings for the sake of others, in order to be rewarded eternally in this world and the hereafter (Imam Muslim, 1997). As previously mentioned, the definition of *waqf* suggests continuous and sustainable nature of *waqf* assets. Accordingly, the concept of *waqf* can only be applied on non-perishable property, which benefit can be extracted from it without consuming the property itself. Among these types of property include real estate, stocks, cash money, books, and chattel (Hassan & Shahid, 2010).

Issues of *Waqf* Management in Malaysia

The Federal Constitution of Malaysia confers the management and administration of *waqf* to be under the state jurisdiction. Hence, all affairs relating to *waqf* in Malaysia is administered by the 14 different Islamic Religious Councils (SIRCs). The SIRCs act as the sole trustee for all *waqf* properties in every state in Malaysia as evident in all state Enactments/Act. The SIRC as the *mutawalli* (sole trustee) is responsible in preserving *waqf* properties, maximizing their revenue and distributing the benefits derived from the *waqf* according to the specified objectives of *waqf*.

It can be fairly said that the diverse set of legislations and Islamic rulings (*fatwa*) endorsed and adopted by the 14 different states have made the effort to develop *waqf* properties in Malaysia a challenging task. Dissimilarities in the *waqf* governance adopted by these states highlight the need to have a standardized *waqf* management throughout Malaysia in order to improve the quality of *waqf* management as a whole (Isa et al., 2011). Though this burning issue has been taken care of by the Federal Government through the establishment of the Department of *Waqf, Zakat and Hajj* (JAWHAR), many works are still needed to streamline the management of *waqf* development in this country.

Since, the roles of *waqf* institutions are not given proper attention, a lot of *waqf* properties are ill-managed (Hassan & Shahid, 2010). For instance, 2014 statistics issued by the Department of *Waqf, Zakat and Hajj* showed that from the 11,000 hectares of *waqf* land worth more than RM1 billion in Malaysia, but only 0.72% of it has been developed. Hence, despite having the potential of contributing to the improvement of society, a substantial amount of *waqf* assets are still lying undeveloped across Malaysia, and arguably throughout the world. Abdul Halim et al. (2014) suggested that the problems that arised regarding *waqf* management can be identified in two areas: the procedure of the daily operations of *waqf* management; and lack of economic growth. Some other fundamental issues, identified which have hampered the development of *waqf* institutions in Malaysia, include lack of funding and expertise, ineffective management of organisation, incomprehensive law as well as scattered and uneconomical size of *waqf* assets to be used for development.

It is without a doubt that *waqf* is a very powerful concept that is a flexible and dynamic mechanism, with a variety of assets that are able to serve the interests of mankind in this world and the hereafter. There are two major types of *waqf* assets; the first one is related to fixed properties such as land and homes while the other one is pertaining to cash which is more liquid compared to the former. Aminah and Sabit (2011) analysed the weaknesses of various methods used in developing *waqf* assets. They concluded that most of the proposed or implemented mechanisms suffer from two major problems: inadequacy of *waqf* funds (in terms of cash) and the illiquid nature of *waqf* assets, which will inevitably hinder the subsistence and sustainability of *waqf* institutions. Such 'rich asset, cash poor' scenario has raised concerns among the stakeholders of *waqf* in the quest of finding the viable and innovative mechanisms to develop unattended and stagnant *waqf* assets.

Waqf Governance: From Charitable Waqf to Corporate Waqf

The institution of *waqf* is primarily instituted to serve two objectives. From a spiritual perspective, *waqf* provides a vehicle for perpetual reward for the *waqif* (donor). On worldly benefit, it offers socio-economic benefits to the whole community in general, and to society's underprivileged society in particular (Mohammad Abdullah, 2015).

Throughout the centuries, most of the charitable *waqf* have been managed by individual *mutawalli* or institutional *mutawalli* where the institution serves as a non-profit organisation (NPO). However, *waqf*, like other institutions in the non-profit sector have survived self-regulations with minimal or even without external oversight. Compared to for-profit or commercial entities that are obliged to produce financial reports in line with certain financial reporting standards, not-for-profit organisations are relatively less regulated and subject to minimal financial reporting requirements (Cordery & Baskerville, 2007).

With the rapid development of Islamic finance, the modern trend in the *waqf* industry is to appreciate the institutional management of collectively pooled *waqf* properties (Çizakça, 2011). Apparently, there has been a shift in paradigm in both the process of creating *waqf* and in the parameters of their management. Remarkably, due to the marked changes in the means, methods, mechanisms and management of modern *waqf* donations and their administration, the demand to explore the corporate structure of *waqf* and its governance framework is bound to rise across the board (Mohammad Abdullah, 2015). The governance of *waqf* institutions will only be considered successful if the necessary duties are performed with accountability and transparency in its operations, together with the necessary reporting requirements. In essence, proper governance of *waqf* that promotes transparency and accountability is important, as *waqf*, is in fact a sector which relies heavily on the confidence and trust of its stakeholders.

Corporate Waqf

Corporate *waqf* is one of the modern mechanisms invented for the management of *waqf*. In this mechanism, *waqf* assets are generated in the form of cash *waqf*, *waqf* shares and other asset-generating methods, before the accumulated assets are invested into various investments instruments in a professional manner. Dahlia Ibrahim and Hasnidar Ibrahim (2013) summarized that this mechanism is a combination of the perpetuity characteristic of *waqf*, together with the power entrepreneurial dynamism. Therefore, for corporate *waqf* to be successfully adopted, it is important that the practice of entrepreneurship, governance, leadership, accountability and

transparency in the corporate sector are implemented. There are five principles and objectives of corporate *waqf*, namely: (1) to create an Islamic institution catering to society's need for elements of corporate entity; (2) to carry out the responsibility to the *ummah* for eternity; (3) to voluntarily share wealth, time and expertise; (4) to generate wealth and to protect incomes; and (5) to establish an incorporation instrument that is trustworthy and wholly (Ministry of Finance, 2011).

In 2006, JCorp launched the 'Corporate *Waqf*' initiative, which involved the transfer of its shares as *waqf* to Kumpulan Waqaf An-Nur Bhd as their trustee (JCorp, 2007). This concept is a key institutional strategy for achieving its corporate mission of '*Jihad Bisnes*'. As proof, via its corporate *waqf* agenda, JCorp pledges to dedicate 25% of their annual dividend pay-out from the shares transferred to *waqf* under the *fi sabilillah* initiative that includes healthcare, education, entrepreneurship aid and other charity programmes (JCorp, 2007). Based on the *waqf* deed, 70 per cent of the dividends from the shares that were under *waqf*, will be used for reinvestment in Islamic fixed deposits and expenses for human resource development, while the remaining 5 per cent was disbursed to the Islamic Religious Council of Johor and the remainder was distributed to beneficiaries.

Additionally, in June 2017, JCorp embarked on another agenda of corporate *waqf* with the launching of Waqaf Saham Larkin Sentral, which offered RM850 million at RM0.10 sen per unit that were opened to both the Muslims and non-Muslims. The Waqaf Saham Larkin Sentral is to be offered through *Waqaf An-Nur Corp Bhd*, a JCorp subsidiary, for the redevelopment of Larkin Sentral Transportation Terminal and of wet markets with development values of RM85 million (Waqaf Larkin, 2017).

Undoubtedly, *waqf* institutions that are professionally managed can significantly contribute towards improving welfare standards and the quality of life of many, especially the beneficiaries. Thus, ongoing research pertaining to contemporary methods of structuring and managing *waqf* assets (Kahf, 1998) is always high in demand. Subsequently, the previous discussion provides a dire and valid justification for considering the integration of Islamic capital market instruments to the development of *waqf* assets, including that of Islamic real estate investment trusts (I-REITs).

The Landscape of Islamic Real Estate Investment Trusts (I-REITs) in Malaysia

Islamic real estate investment trusts (I-REITs) is a collective investment instrument (similar to mutual fund/unit trust) that uses fundraising from investors for the purpose of buying, managing, or selling of property such as houses, commercial buildings, farms, and car parks (SC, 2006) or other financial assets related to property such as a company's stock and *sukuk* issued by real estate companies (SC, 2007). Thus, I-REITs itself is a company that owns and usually manages commercial or residential property like apartments, offices and factory spaces, for the shareholders.

Malaysia is the first jurisdiction in the global financial sector to issue the Guidelines on I-REITs (SC, 2006) and has been set as the global benchmark for the development of I-REITs. The 2008 Malaysia's Securities Commission guideline on REITs stipulates that REITs must invest at least 50 per cent of its total assets in real estate, whether via direct ownership or through a single purpose company whose principal assets comprise of real assets. This allows the shareholders to invest in property without actually having to own the property outright (Dusuki, 2011).

The major advantage of I-REITs is that it is much easier to buy, or sell shares in I-REITs, which are traded on major exchanges than to buy, or sell property in the traditional way. REITs or I-REITs are viewed as the best combination of investment in real property and stocks (Anuar & Soi, 2011). The return is indeed lower than investing in stocks but would be more stable as it generates steadier incomes for long term investments. This is the uniqueness of investing in REITs and the awareness of this profit-driven investment tool has been raised recently. The holder of one REITs unit is actually buying a fraction of a managed pool of real estate (Anuar & Soi, 2011), which entitles the unit holder to the beneficial ownership of or beneficial interest from the real estate in terms of right to receivables. Moreover, this securitized real estate provides periodic returns to investors due to the increase in value of property owned. The returns or dividends of REITs are generated from rental income and added with capital appreciation of property assets throughout the holding period (Anuar & Soi, 2011).

Malaysia has been hailed as the pioneer of I-REITs development with the launch of the first instrument of its kind in the world namely Al-'Aqar KPJ REIT in the year 2006 (Newell & Atasya, 2009). This was followed by Al-Hadharah Boustead REIT and AXIS REIT both in 2007 and 2008 respectively. However, *Al-Hadharah Boustead REITS* had been privatised in 2013, which involved the redemption of all units in Boustead REIT held by the unit holders in an attempt to consolidate the plantation assets under Boustead Holdings (*The Star*, 2013).

In May 2013, the KLCCP-*i*, a stapled-security which consists of equity and I-REITs, was established. The recent establishment of these stapled REITs has contributed towards a significant growth of market capitalization of I-REITs in Malaysia from RM3.64 billion to RM15.4 billion in 2013 (SC, 2013). In 2015, Johor Corporation's Al-Salam REITs was listed in Bursa Malaysia as the fourth I-REITs in Malaysia with market capitalization of about RM600 million and a property value of RM922 million. *Al-Salam REIT* is a diversified Islamic REITs consisting of a four-level shopping mall serving retail, office premises and food and beverage segments in the southern region of Peninsular Malaysia, Johor. The launch of I-REITs has embarked the introduction of another form of ethical investment, which has provided an opportunity for Muslim investors around the world to diversify their investment portfolios to generate returns and improve profitability based on the principles of *Shariah*.

On a global level, there is a large untapped market for I-REITs and Malaysia has an advantage over the rest of the region providing new opportunities for market players, including fund managers, to further diversify their investment portfolios. With an established regulatory framework that facilitates the creation of a new asset class, this provides a huge opportunity for Malaysia to attract foreign investors especially from the Middle East, to invest in this country. This was evidenced in the case of Al-'Aqar Healthcare REIT (formerly known as Al-'Aqar KPJ REIT), which successfully attracted Middle East investors to support it via a \$100 million syndicated *ijarah* facility after its launch in 2006 (Newell & Atasya Osmadi, 2010).

As for the sponsor, I-REITs has the potential to attract a wider pool of institutional and individual investors to help support the

expansion of the property sector by acquiring more property into the structure and to stimulate the industry. The proven ability of REITs to raise equity capital may also provide funding for upgrading and maintaining the infrastructure and facilities of various forms of asset classes such as airports (Messer, 2011) and healthcare institutions. The whole idea is in line with the fundamental role of a financial market as a platform that mobilizes the capital from the sector that has surplus to those that have a shortage of funds. This may also result in a more enhanced level of economic efficiency in a country which allows funds to move from those who lack productive investment opportunities to those who have such opportunities (Mishkin, 2010).

Features of *Shariah* Compliant REITs

In 2005, the SC introduced Guidelines on Islamic REITs which is the first of its kind in the world. The most important feature of I-REITs is the appointment of a *Shariah* committee or advisory panel that is responsible to watch over the process of I-REITs to ensure that it conforms to *Shariah* principles. The distinguishing feature of I-REITs is its classification as an ethical investment that prohibits non-*halal* or non-permissible rental activities such as financial services based on interest (*riba*), gambling/gaming, manufacture or sale of non-*halal* products or related products, conventional insurance, leisure activities that are non-permissible according to *Shariah*, manufacture or sale of tobacco-based products or related products, stockbroking or share trading in non-*Shariah*-compliant securities and hotels and resorts.

The inception of I-REIT started with the process of acquiring a new property into the I-REITs portfolio. For a tenant with mixed operation activities involving *Shariah*-permitted activities and *Shariah*-forbidden activities, the fund manager needs to perform some additional compliance assessment. The requirement is that the rental from non-permissible activities should not surpass 20 per cent of total turnover of the I-REITs in the current financial year. If it does exceed the 20 per cent benchmark, the *Shariah* advisors will advise the property manager against acquiring and investing in the property. For renting out to a new tenant, the 20 per cent benchmark is not applicable in cases where the new tenant engages in activities that are clearly considered impermissible. I-REITs companies should also

ensure that all types of investments, deposits and financing instruments should conform to *Shariah* principles.

The I-REITs guidelines also specified that I-REITs are obliged to employ *takaful* schemes to insured its real estate. Nevertheless, in the case of the *takaful* schemes are incapable of providing the insurance coverage, the I-REITs are permitted to take conventional insurance, provided that prior approval from the *Shariah* advisors has been obtained. I-REITs are also allowed to take part in forward sales or purchases of currency for the purpose of hedging its position. In this respect, I-REITs shall involve themselves only in *Shariah*-compliant hedging instruments. Only if the Islamic instruments are not commercially viable, will I-REITs be allowed to obtain *Shariah* non-compliant instruments, with the provision of approval being obtained from the *Shariah* advisors.

DISCUSSION AND FINDINGS

Is the *Waqf* Concept and I-REITs Viable?

The *waqf* concept emphasises on having the sustainable incomes for the *waqf* properties to be distributed to beneficiaries. Thus, the effort of developing abandoned or under-developed *waqf* properties by means of efficient and dynamic structures should be given high priority by the *mutawalli*. In fact, there are many *waqf* properties that have yet to be exploited in generating more income and benefits for the *maslahah* of the *ummah*.

The Implementation of 'Internal REITs' in Singapore

The Islamic Religious Council of Singapore (MUIS) has creatively invented an 'internal REITs' for its *waqf* assets. This was done through the purchase of a six-level office building at 11, Beach Road where an asset migration exercise was undertaken. *Waqf* assets with low value and yield were transferred to a high yielding asset through the *istibdal* process. The net returns from rental of buildings were then distributed to the *waqf* beneficiaries based on their shareholdings in the asset (Shamsiah, 2010). At present, the beneficiaries of *waqf* assets with low returns prior to the migration process have become the shareholders to high quality assets with better yield. The net assets value of the property increased from \$25 million in year 2007 to \$100 million in

year 2012 (Shamsiah, 2012). As a result, MUIS was able to give more benefits to the trustees or administrators as well as the beneficiaries, which among them, include the increase in asset value due to the strategic location of the assets after migration, proficient management, and high sustainable incomes. It should be noted that income generated from *waqf* is also channeled into providing education to the targeted groups and the needy.

The Implementation of *Waqf* of Shares by Johor Corporation Berhad

Malaysia is the global pioneer in establishing I-REITs with the launch of Al-‘Aqar KPJ Healthcare REITs (formerly known as Al-‘Aqar KPJ REIT) in August 2006, which comprise six hospitals in the portfolio. Since its inception, the number of properties has increased from six assets to 25 assets with the primary focus being on healthcare-related properties such as hospitals, nursing colleges and retirement living facilities. The values of these properties have increased approximately three times from RM 486 million in 2006 to RM1.4 billion in the year 2012 (Damansara REITS, 2012). By implementing the I-REITs mechanism, Johor Corporation Berhad (JCorp) that is the sponsor, has also managed to raise funds from the investors to expand their healthcare business in terms of financing new medical equipments and facilities (Ngadimon, 2011), upgrading buildings as well as acquiring more hospitals in order to enhance the size of their investment portfolio.

Additionally, in 2009, WANCorp, a subsidiary of JCorp, which is responsible for managing *waqf*, took a drastic move to tackle the issue of depreciating value of *waqf* stocks by replacing underperforming shares with outperforming shares through the *istibdal* (substitution) process. The *istibdal* process involved the replacement of Johor Land Berhad shares with 12.62 million to Al-‘Aqar Healthcare REITs shares that were worth RM13 million. This exercise is a clear evidence that ‘*waqf* REITs’ have already indirectly taken place in Malaysia although the volume is found not to be very significant and has not been officially announced by JCorp. The contribution of *waqf* REITs along with *waqf* of shares under the label of corporate *waqf* has contributed towards the socio-economic well-being of Muslims and non-Muslims. This initiative came together with

various important actions including efforts to implement corporate social responsibility (CSR) initiatives in managing hospitals, clinics, mosques, entrepreneurship and educational programmes, which are all based on the *waqf* concept. Apart from that, contributions were also extended to the international level through the Somalia Humanitarian Aid and GAZA Humanitarian Funds in 2011.

From these two examples, it is observed that the synergy of innovation and creativity by highly talented and motivated people, coupled with progressive *fatwa* and easy access to finance, together with a robust legal framework and strong governance, have contributed towards the successful management of *waqf* assets by MUIS and WANCorp. Corresponding to this advancement of *waqf* management in Singapore and the dynamic role of stock *waqf* in socio-economic development in the state of Johor, further research to analyse the potential of I-REITs structure in *waqf* development in Malaysia is then crucial, particularly in bringing in more innovation and expertise towards pursuing *waqf* growth to the next level.

Views of *Shariah* Experts on *Waqf* REITs

According to Hasan (2014), the concept of *waqf* REITs is not feasible to be implemented in the current Malaysian legal framework since the REITs guidelines stipulate that the establishment of REITs can only be realised by selling the assets in the form of units to REITs investors. This approach, however, contradicts with the underlying principles of *waqf* which dictates that the *waqf* asset should not be transferred out of *waqf* ownership through any buying or selling activities or even be given as *hibah*.

Hence, for it to be viable, two aspects need to be dealt with. First, the *waqf* REITs should have a certain maturity date that shall be specified in the deed (Clause 15.21 of the *Guidelines on Real Estate Investment Trusts*), where SIRC shall buy back the *waqf* assets after a certain period of time. Second, a *Shariah* resolution should be passed to decide whether the temporary sale of *waqf* assets to the investors in REITs is acceptable and does not contradict the *Shariah* ruling of non-disposal of *waqf* assets. Whilst the first issue can easily be met, the second issue needs a proper *Shariah* discussion to decide on the matter. If the decision is in the affirmative, proper parameters need to

be established to ensure that the *waqf* assets will definitely be reverted back to *waqf* and the right of the SIRC in the *waqf* assets would not be jeopardised. Perhaps, in the light of the non-existence of this *Shariah* Resolution on this matter, the application of an *ijarah* contract for a long-term period or *al-hukr* (long-lease) may be regarded as a viable option to the current practice, with no provision that the current law is amended to allow the establishment of *waqf* REITs based on lease and lease back.

Bakar (2014) is of the view that I-REITs is a viable model to finance the development of *waqf* through the offering of units to the investors where the capital raised can be used to refurbish the existing buildings or to establish new *waqf* assets. This can be realised through a specific clause in the agreement between the SIRC as a trustee and the I-REITs where the SIRC will buy back the *waqf* assets that have been 'sold' to I-REIT after a certain period of time, for example 30 years. He added that in this situation, there is no issue that the ownership of the *waqf* property might be transferred to any third party as it is secured by a clause where the assets would be bought back by SIRC after the maturity period. This mechanism is to allow *waqf* assets that have no liquidity to be "sold for a while" for the purpose of obtaining capital to finance the construction or upgrading the infrastructure on the basis of preserving the *maslahah* of the *waqf* itself. Ngadimon (2011) also shares the same view on the viability of I-REITs structure in financing and expansion of *waqf* assets in Malaysia for the well-being and advancement of the Muslim community. Figure 12.1 illustrates the proposed structure of *waqf* REIT.

Figure 12.1: Proposed Waqf REIT Structure

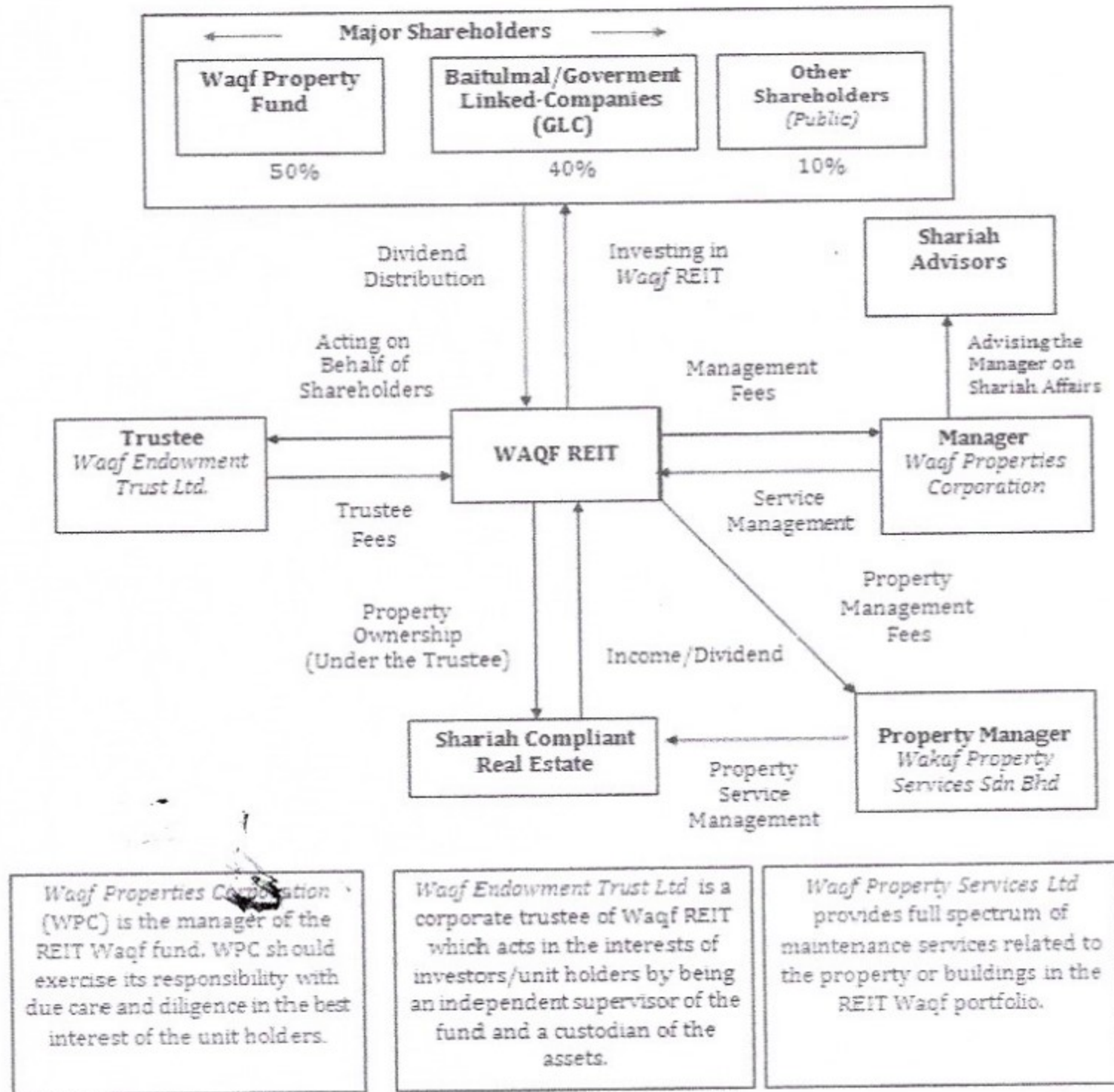


Figure 1: Proposed Waqf REIT Structure

PROPOSED WAQF REITs STRUCTURE

In this structure, a REIT will be established by the SIRC as their sponsor. Suitable income generating assets will be identified and be injected into waqf REITs. The REITs manager will offer the REITs units to various entities, which includes the Waqf Property Fund, Baitulmal, GLC as well as the public. These investors will purchase units of waqf REIT, whose proceeds will be used to refurbish the existing waqf assets or to purchase new Shariah-compliant assets for the expansion of the waqf REITs portfolio that are previously identified by the SIRC. The assets will be leased backed to the SIRC. SIRC will then sublease the assets to the Shariah-compliant tenants. The

returns from the tenancy will be distributed to the investors. The dividends gained from this *waqf* REIT will then be used for charitable *waqf* purposes and activities for the benefit of the *ummah*. At the end of a certain agreed period, the SIRC should be allowed to purchase back the asset at par value and hence, resulted in the termination of the Islamic REITs.

In summary, it should be noted that the establishment of *waqf* REITs will mark the creation of a new asset class of *waqf*. This initiative is in line with the resolution by *Majma' Fiqh* in 2009 on the permissibility of *waqf* of financial rights (*huquq al-maliyah*) that are *Shariah*-compliant such as the company shares, *sukuk* and intangible rights (*huquq ma'nawi*) that comprise intellectual property such as copyrights, trademarks and patents along with *waqf* of unit trusts (Al-Majma' al-Fiqh al-Duwali, 2009).

CONCLUSION

In the current competitive global economy, the search for a new mechanism that integrates Islamic finance and *waqf* sectors has brought a new array of development in the Muslim world. The convergence of these two *Shariah* compliant sectors is promising to be a new engine of growth and quantum leap that engages more Muslims to an efficient and systematic way of managing *waqf* assets. This chapter submits that I-REITs structure has the potential as a source of social finance particularly in financing the development of abandoned, under-developed and scattered *waqf* assets by unlocking the values of *waqf* assets without losing ownership over the property. This new corporate *waqf* concept, which is conceptualised as *waqf* REITs, will contribute to *waqf* in three ways: first, generating a large amount of capital through temporary selling of a pool of *waqf* assets in which the proceeds of this temporary disposal can be channeled into refurbishing of existing *waqf* assets or acquiring new *waqf* assets; second, ensuring sustainable return to *waqf* beneficiaries through periodic dividend payments; third, elevating the traditional management of *waqf* into good corporate governance by professional and experienced managers.

The implementation of the model has yet to be tested under current governing laws in Malaysia. SC has so far pledged a strong commitment to provide professional advice on social responsibility

investment (SRI) initiatives including *waqf*. With the new release of the Malaysian Code on Corporate Governance (MCCG) by SC, it is hoped that this will accelerate the best practice of *waqf* governance in the arena of the Islamic capital market. Besides that, in conceptualizing *waqf* REITs as a fast growing Islamic equity market, further research needs to be carried out to harness the potential of I-REITs as a viable instrument to develop *waqf* assets. Thus, the proposed conceptual framework of *waqf* REITs can be a catalyst and an effective tool for policymakers, *waqf* managers and future researchers to restore the core functions REITs. Researchers should study new product innovations and development using REITs structure. In essence, the chapter has sought to fulfill continuous the dual aspirations of Muslims in preserving worldly norms while gaining the eternal rewards in the hereafter.

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