

“ The Regulation of Globalized Islamic Finance”

Qatar Islamic Bank

Friday, December 05, 2008

Private and confidential. Do not circulate.

Contents

1. Islamic Finance overview
2. Legal Barriers
3. Opportunity for Islamic Finance in France
4. QIB Strategy

Islamic Finance - A fast growing niche

- Growing at around 20% per annum, the industry is estimated to stand at US\$ 700bn currently (Moody's) with Islamic assets set to reach US\$ 4tr by 2013 (S&P)
- Islamic bond market has grown 85% since 2001 and new issuance is set to exceed US\$ 100bn per annum in the next few years (S&P and Euroweek)
- Concentrated, but not confined to, the Middle East and South East Asia
 - China- US\$ 250mn sukuk for power project;
 - Germany- Saxony-Anhalt €100mn sukuk;
 - Khazakhstan- Bank TuranAlem US\$50mn financing;
 - UK- Aston Martin LBO & HM Treasury planned sukuk issuance;
 - USA- US\$ 165mn sukuk for East Cameron Texas

Friday, December 05, 2008

Private and confidential. Do not circulate.



Legal Barriers for Islamic Finance in France

- Islamic and conventional banks do not compete on a same level playing field. Numerous tax and legal restrictions can constitutes barriers for Islamic Finance in France.

1- TAX restrictions

- In many jurisdictions, Islamic real estate financing through the diminishing Musharakah technique leads to a double taxation with conveyance duty on the acquisition of the real estate.

- Islamic mortgages attracted double stamp duty. Both of the property by the bank and on the transfer of the property by the bank to the customer at the end of the mortgage terms → any changes would be a matter of public policy.

- The selection of the jurisdiction governing the deal will determine the tax implications such as VAT, corporate taxes, taxes on dividends, transfer taxes on the asset sales, stamp duty, etc...

Example: The Murabaha transaction for example introduces two sale contracts each of them is liable to tax. When structuring a deal, great attention should be drawn up as to the tax implications as many of the jurisdiction are still not Islamic Finance tax friendly.

France should probably follow the UK example who since 2003, made a number of legislative amendments in favor of Islamic finance which enables this particular industry to grow in the U.K.

2- Legal restrictions

Contracts:

- In the Islamic transactions contracts, the enforceability of terms and conditions depends on the governing law

In case of a dispute, it is unlikely that the French court will give a verdict based on Sharia law => To mitigate this risk, contracts have to be written very carefully to minimize potential disputes and state the governing law.

A standardization of documentation and a number of initiatives are required and under way in this field.

- Due to non-presence of a formal litigation system, dispute settlement is one of the serious risk factors in Islamic banking.

But in ought to overcome such risks, the counterparties can contractually agree on a process to be followed if disputes become inevitable. This is particularly significant with respect to settlement of defaults, as interest-based debt rescheduling is not possible.

•Financial transactions:

-This is a core issue, and one of great importance in many Muslim countries. It has no real equivalent in non-Muslim societies, and in a broader sense raises fundamental questions about the organization of society.

Generally, this only becomes a problem when a transaction goes wrong, and the parties end up in dispute. But transactions routinely do go wrong, and as Islamic finance grows, Courts in France are going to have to find an appropriate response to the possibility that the application of the Sharia' and that of a secular system of law will not necessarily produce the same outcome.

-Different lending structures may generate different risk and balance sheet exposures for Islamic banks.

-The treatment of profits and losses may have consequences for the balance sheet structure.

- The disclosure requirements may need strengthening so that investors can make decisions based on their risk preference.

- New-Products Legal Analysis:

Legal and Sharia' counsels, either in-house or outside of the Islamic Financial Institution, should be involved in the new-product or structure approval process. New-product reviews should include products being offered for the first time in a new jurisdiction or to a new category of counterparties. The definition of a new product should be consistent with the size, complexity, and sophistication of the institution. Small changes in the payment formulas or other terms of products can greatly alter their risk profiles and justify designation as a new product.

Examples of Non Muslim Countries Supporting Islamic Finance

. Hong-Kong:

- The City State is a new comer into the Islamic Finance world, its objective is to be the gate way for Islamic investors, mainly from the Middle East, to mainland China
- HK started to be an observer into the Islamic Financial Services Board, the international body established to develop standards for Islamic Finance, and recently raise its status to associate of the institution

Examples of Non Muslim Countries Supporting Islamic Finance

Singapore:

- MAS joined the IFSB in 2003 as an observer and became a full member in 2005
- Since 2005 MAS (Monetary Authority Of Singapore) started to change regulation to enable Islamic Finance to grow:
 - Waived the double imposition of stamp duty on real estate financing which has been structured under Sharia'a law
 - Accorded the same concessionary tax treatment on income from Sukuk that are applicable to conventional bonds
 - Allow Singaporean banks to offer Murabaha financing
- Creation of an Islamic Bank in Singapore (2007); Islamic Bank of Asia
- Singapore will issue its first sovereign Sukuk in 2009

Examples of Non Muslim Countries Supporting Islamic Finance

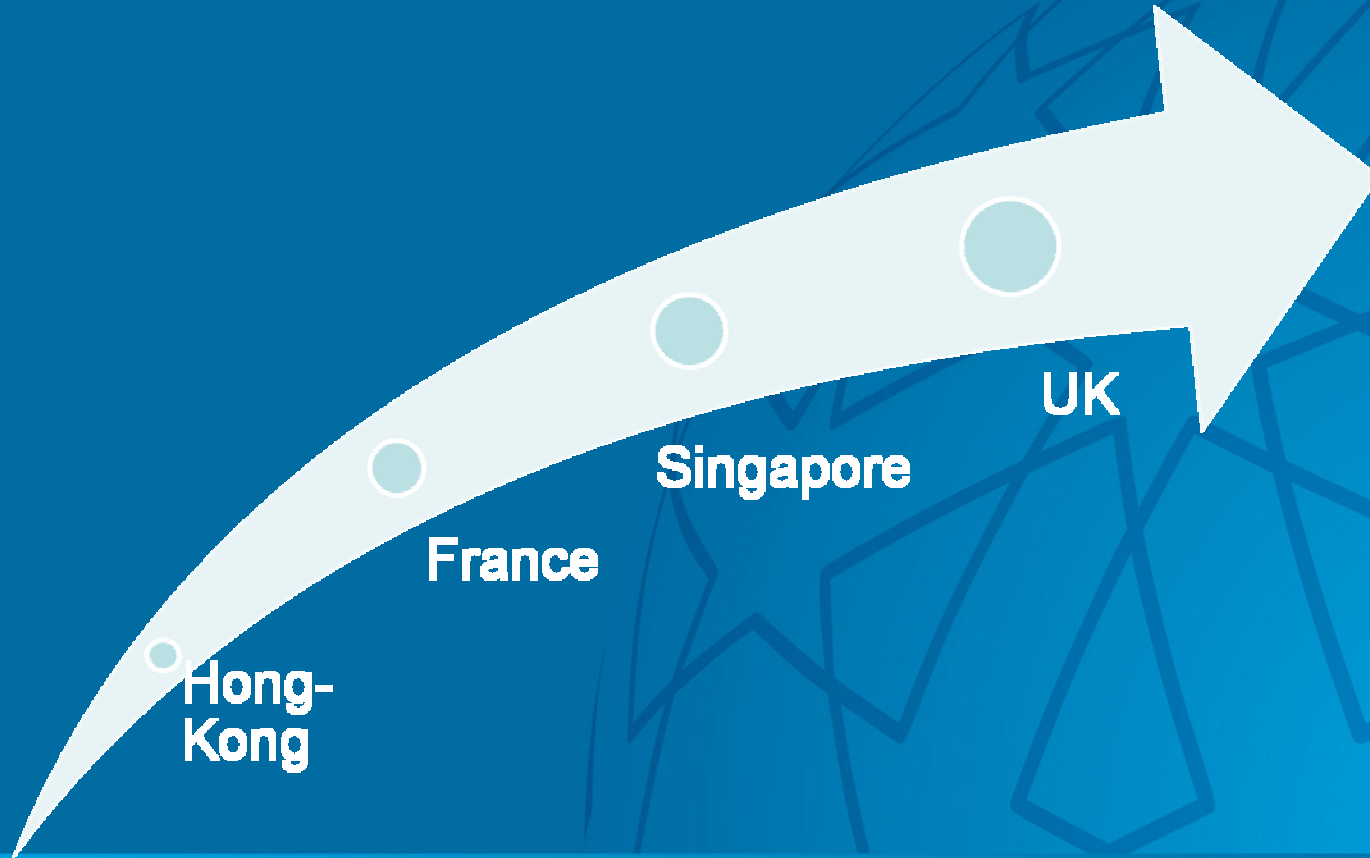
UK:

- Since the early 2000s the UK government has introduced a series of tax and legislative changes specifically designed to remove obstacles to the development of Islamic Finance;
 - The first significant change came in the Finance Act 2003 which introduced relief to prevent multiple payment Stamp Duty Land Tax on Islamic Mortgages
 - The Finance Acts 2005 and 2006 contained further measures aimed at putting other Islamic products on the same tax footing as their conventional counterparts.
- All the main UK banks are proposing Islamic products to their clients through Islamic windows in top of the Islamic banks operating in the UK (European Finance House, Islamic Bank of Britain...)
- The UK government is considering issuing a sovereign Sukuk

Steps taken by France to encourage the Islamic Finance

- . France has proven it's keen to encourage the development of Islamic Finance
- . Recent months have also seen enormous work by practitioners to identify hurdles to the development of Islamic Finance products in France in particular within think tank.
- . As a result, both French ministry of economy, Industry and Employment and the Autorité des Marchés Financiers (AMF), the French financial markets regulatory authority, announced on 2 July 2008 significant tax and regulatory changes aimed at boosting Islamic Finance in France.
- . These changes relate to the listing of the SUKUK in France, the tax treatment of Islamic Finance transactions and reforms regarding “fiducie” or French trust.

France in the learning curve



Qatar Islamic Bank Strategy

Friday, December 05, 2008

Private and confidential. Do not circulate.



A dynamic international network



8 locations at present
16 locations by 2012

Friday, December 05, 2008

Private and confidential. Do not circulate.

QIB expansion into France is in the core of the French Qatari bilateral long term economic cooperation

Creation of European Finance House France



**QIB follows
Qatari
Foreign direct
investment**

**QIB great
International
Network**

**QIB great
expertise in
Islamic Finance**

**QIB strong links
with Qatari
corporates – the
banks' clients**

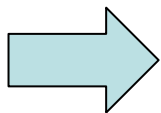
How will France benefit from exposure to sharia-compliant Finance

1. Opportunity for France to play a more active role in the field of compliant Finance

- Could be positioned as the Link between the UK (at present European Centre for Islamic Finance) & Continental Europe
- Gate for French speaking Countries (future potential sharia-compliant Finance Markets)

2. Opportunity to tap new markets and sharia-sensitive investors

- Additional debt markets
- Additional capital markets
- Additional sharia-sensitive investors



Access to more liquidity

Our strategy in France

- Open European Finance House France by 2010.
- Duplicate whenever possible QIB expertise in France in several areas mainly Corporate and Investment banking, Asset Management and Private Equity.
- Trigger Qatari investments in France => **through QIB big network of private and institutional clients who wish to expand into France mainly in Real Estate, Infrastructure, Energy.**
- Offer more sophisticated sharia compliant products and services such as Ijara Financing, debt capital market products, and asset management products as per the Turkish banking requirements. (i.e. long term financing schemes)
- Develop **Sharia-compliant mortgage financing and investment (retirement) scheme** for the french population distributed in partnership with a french bank (La Poste/Caisse D Epargne...)
- Finance French Companies in their Qatari contracts

Friday, December 05, 2008

Private and confidential. Do not circulate.



Conclusion

- Minimal legal issues
- Tax issues: Other non Islamic countries solved these issues with few steps
- Political will: France is going in the right direction,
- Opportunities: Strengthen ties between France and GCC countries

Thank you

Friday, December 05, 2008

Private and confidential. Do not circulate.



The only global Islamic banking network, courtesy of QIB

With its affiliate companies, QIB delivers customized Shari'a banking solutions across Europe, the Far East and the Middle East.



QIB was established 25 years ago, making it Qatar's oldest Islamic bank. Through its unwavering focus on quality and transparency, QIB has since gone on to become one of the world's top five Shari'a banks.

Now with its affiliates in Qatar (QInvest) and an affiliate bank each in Lebanon (Arab Finance House), Malaysia (Asian Finance Bank) and the UK (European Finance House), QIB has put together the only global Islamic banking network.

P.O. Box 559 Doha, Call Centre +974 4448444 www.qib.com.qa



Committed to leadership

Annex

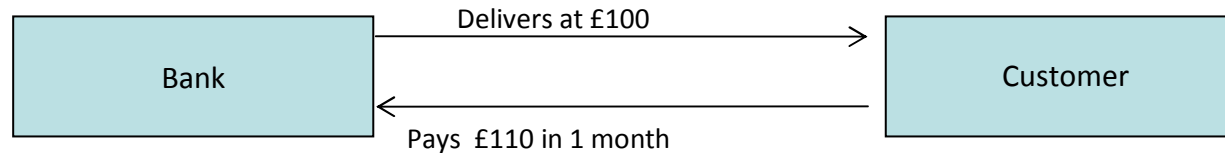
Friday, December 05, 2008

Private and confidential. Do not circulate.



Asset based finance- murabaha

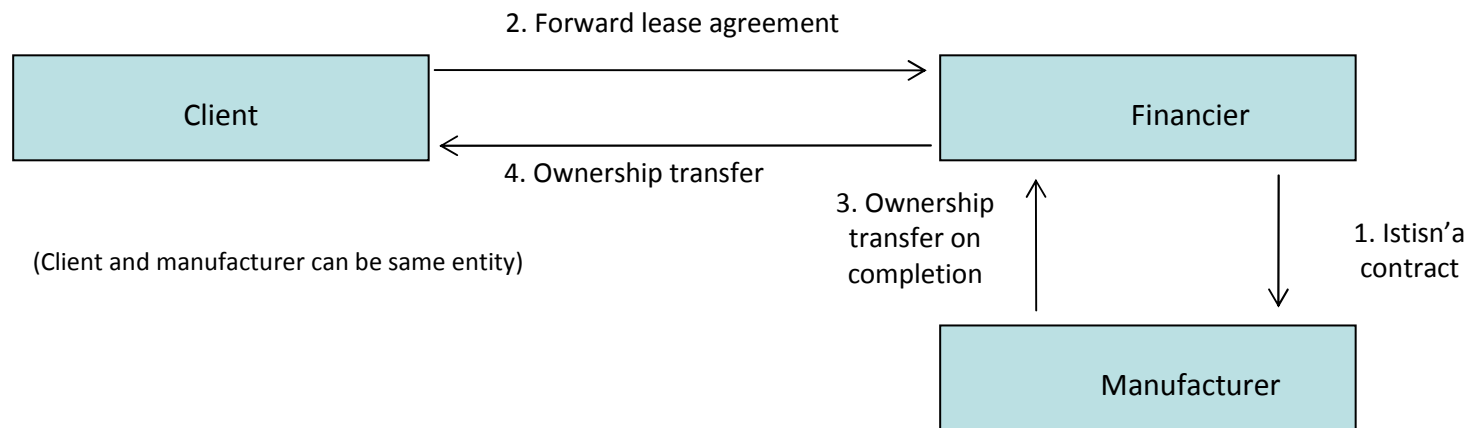
- Deferred payment sale
- Sale of goods with cost price, mark up and payment date clearly defined



- Goods must not be prohibited, must exist and owned by seller and defined
- Deferred payment can be supported by mortgage or pledge
- Deferred amount linked to any benchmark, such as LIBOR
- Mainly used for working capital and trade finance purposes

Asset based finance- istisn'a

- Party seeking funds undertakes to manufacture or construct an asset according to agreed specifications, delivery options and price
- Payments linked to progress and can be deferred



- Financier usually unwilling to hold asset after completion and enters into parallel sales contract with ultimate buyer
- Applications in project & infrastructure finance and pre-export finance

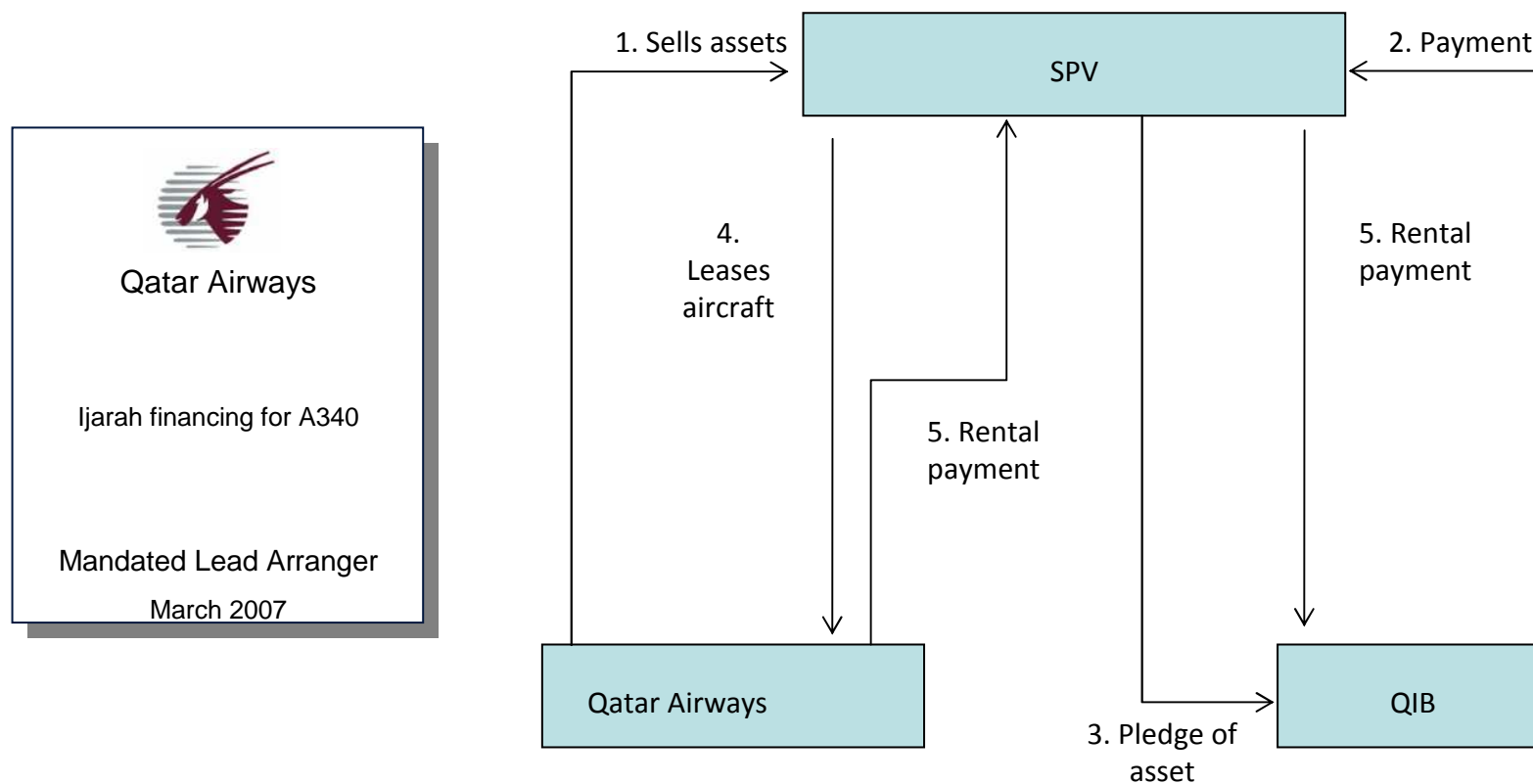
Asset based finance- salam

- Spot payment for future delivery of commodities
- Unlike murabaha, agreed price is paid fully in advance for future delivery
- Goods must be commodities freely available in market and fungible
- Exceptionally,
 - at time of contracting goods need not exist; and
 - seller need not have valid ownership of the goods
- Tool for pre-export finance and working capital financing

Asset based finance- ijara

- Islamic leasing- a bilateral contract allowing transfer of usufruct and/or legal and/or beneficial ownership
- Characteristics of operating lease but can be structured to have economics of financial lease through redemption features such as promise to purchase
- Rental payments can be fixed or floating and linked to any benchmark

QIB - Aircraft leasing via ijara



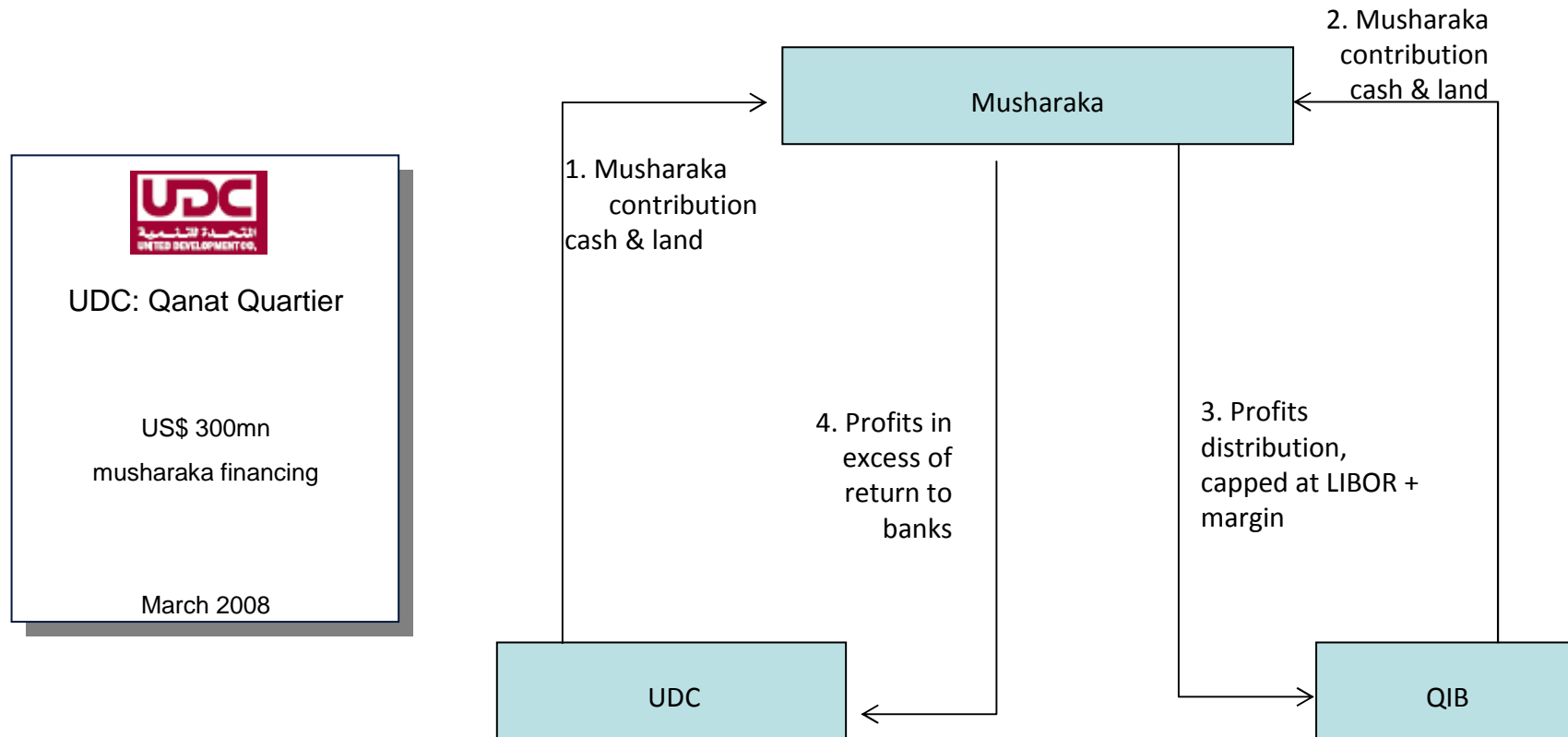
Asset based finance- sukuks

- Equivalent to bonds
- Represents ownership in underlying assets, unlike bonds which are primarily unsecured obligations
- Sukuk cash flows mirror bond cash flows
- Similar to bonds in that they are tradable, rateable, available to credit enhancement, compatible to standardisations e.g. Reg S, 144A, etc.
- Mechanism to reach previously untapped pools of liquidity and diversify funding sources

Equity based- musharaka

- Contract based on partnership
- Parties contribute capital in cash or kind
- Each partner liable for losses proportionate to share of investment
- Profits distributed to pre-arranged formula, which does not have to follow same proportion of equity
- Guarantee of returns not permitted, returns must be based on profits of venture
- Used to finance real estate, pre-export finance and working capital requirements

QIB -Real estate project finance via musharaka



Equity based- mudaraba

- Partnership where one partner contributes financing and the other, the manager, invest expertise
- Manager invests capital according to defined business plan, with no interference from the financier
- Financier has same rights and obligations as a limited partner or investor in mutual fund
- Manager's role is fiduciary and does not share in losses, which are borne by the financier alone
- Profits shared according to pre-determined formula

1- Clarifications as to the legal and transparent requirements for the listing of Sukuk in France

. On July 2008, the AMF published a statement regarding the listing of Sukuk on a French regulated market.

. The AMF acknowledges that Sukuk issues may be structured either as asset-backed and sets out for each type of Sukuk the level of disclosure required in the prospectus.

. The AMF's objectives is to ensure that prospectuses are prepared in accordance with European laws and regulations , in particular with the Commission Regulation (EC) no 809/2004 of 29 April 2004 implementing Directive 2003/71/EC (the Prospectus Regulations) .

. The AMF emphasize that compliance of a bond issue with Shari' a rules does not fall within its ambit. For issuers to document in their prospectus the information which is relevant for their targeted investors .

2. Clarifications as to the tax treatment of Islamic Finance transactions in France

- . Shariah compliant transactions that take place in France are mainly based on Murabaha transactions in the context of property acquisitions.
- . To avoid registration duty being paid twice , most of transactions rely on the application of the merchant dealer regime, according to which a company may buy properties or shares in real estate companies in order to resell them , the acquisition being exempt from registration duties.
- . However, the use of the regime does not provide all the security that it should, since merchant dealers are required to perform at least two operations of purchase and sale with a speculative intention which is difficult to accommodate in Islamic Finance.
- . A softening of the regime would therefore be very useful.

. Several Murabaha transactions have already been implemented in France, their wider development would also be encouraged by a clarification of their tax treatment as far as direct taxes are concerned.

. Similarly , a clarification of the tax treatment of the profit generated by the Sukuk at the level of the issuer and the subscriber would be welcome.

. The French Ministry of Economy , Industry and Employment announced that the French tax administration was ready to confirm the “ interest” nature of the profit margin for Sukuk real estate , through rulings that would be granted on a first come first basis , it being provided that those of the rulings obtained which are made publicly available by the tax administration are then enforceable against said administration by every taxpayer in the same position.

3. French Trust

. In February 2007, the law creating fiducie was enacted and was intended to bridge the gap in French Law created by the absence of the Anglo- American concept of trust. This law , which was expected to provide an adequate tool for banking transactions in general and Islamic Finance in particular , contained significant restrictions on the manner in which a fiducie can be created .

. In August 2008, a law which renders the framework more flexible was enacted.

. With this new law, lawyers will be allowed to act as fiduciaries. It grants to parties to a *fiducie* greater rights to organize contractually the replacement of the fiduciary and the end of the *fiducie*. In addition, some clarifications have been brought to the conditions for the transfer of commercial real estate and receivables to a fiduciary. Further amendments will be made in this area.

QIB - Principal corporate transactions



Qatar Airways

Airbus 340-600

Ijarah Financing

Mandated Lead
Arranger



Qatar Electricity & Water

Ras Abu Fontas A1

Desalination Plant

US\$ 144mn

Istisna/Ijara

Sole Mandated Lead
Arranger



Al Faisal Holding

Corporate Finance

US\$ 850mn

Ijara

Mandated Lead
Arranger



First Finance

Corporate Finance

US\$ 83mn

Syndicated Murabaha

Account Bank



Al Waab

Real Estate

US\$ 350mn

Syndicated Murabaha

Mandated Lead
Arranger



UDC


Real Estate

US\$ 300mn

Musharaka Financing

Mandated Lead
Arranger

QIB - Principal sukuk transactions



Salam Bounian

US\$ 137mn

Mandated Lead Arranger



Dar Al Arkan
Real Estate

US\$ 1bn
Ijara

Manager

URC

URC
Real Estate

US\$ 100mn
Musharaka

Joint Lead Arranger



ALAQARIA
Qatar Real Estate Investment Co.

QREIC
Real Estate

US\$ 300mn
Musharaka

Senior Co-Lead Manager



State of Qatar

US\$ 700mn
Ijara

Participant



DP World

US\$ 1.5bn
Convertible Sukuk

Participant