

Restructuring Sukuk for Project Financing

Majid Pireh

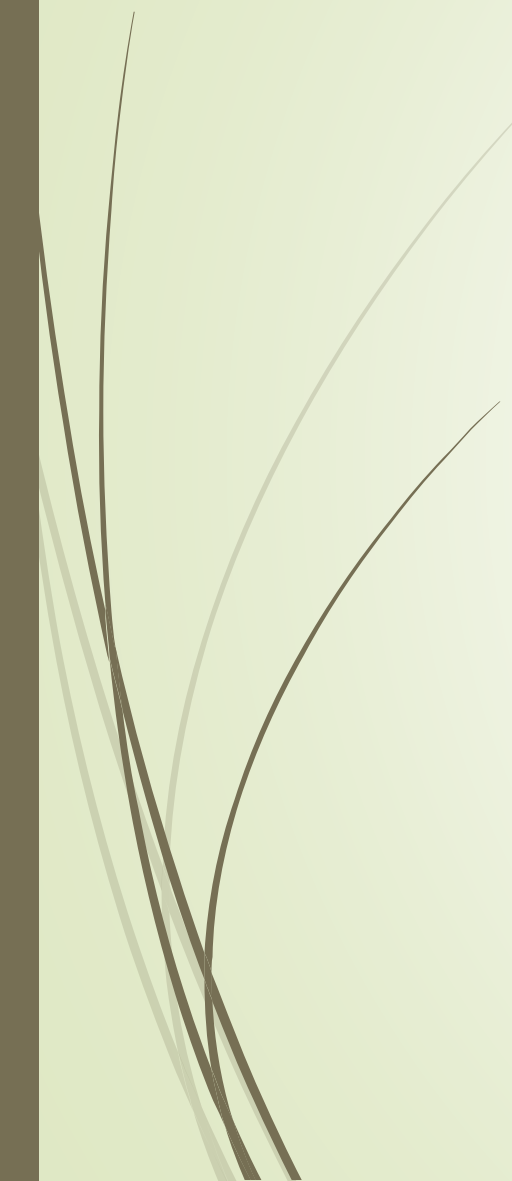
Secretary; Shariah Board of Securities and Exchange Organization
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Project Finance

Definition: a financing method which is composed of different entities to optimally provide financing needs for specific projects

What makes a project finance different from other financing structures?

- Recourse System
- Reimbursement System
- Equity based vs. Debt based
- Long term vs. Short term
- On balance sheet vs. Off Balance sheet
- Time horizon framework



Project Finance





Build-Operate-Transfer (BOT) Structure

- ▶ A famous project finance structure for building new (greenfield) projects
- ▶ In a BOT project, the public sector grants a private company the right to develop and operate a facility or system for a certain period (the "Project Period").
- ▶ Operator finances, owns and constructs the facility or system and operates it commercially for the project period, after which the facility is transferred to the authority.
- ▶ The operator is also prohibited from carrying out other activities. The operator is therefore usually a special purpose vehicle.
- ▶ Project company obtains financing for the project, and procures the design and construction of the works and operates the facility during the concession period.



Build-Operate-Transfer (BOT) Structure (Con 'd)

- ▶ The revenues are often obtained from two sources:
 - ▶ a single "offtake purchaser" such as a utility or government,
 - ▶ pure concession where output is sold directly to consumers and end users
- ▶ Project company obtains financing for the project, and procures the design and construction of the works and operates the facility during the concession period.
- ▶ Project company will co-ordinate the construction and operation of the project in accordance with the requirements of the concession agreement.

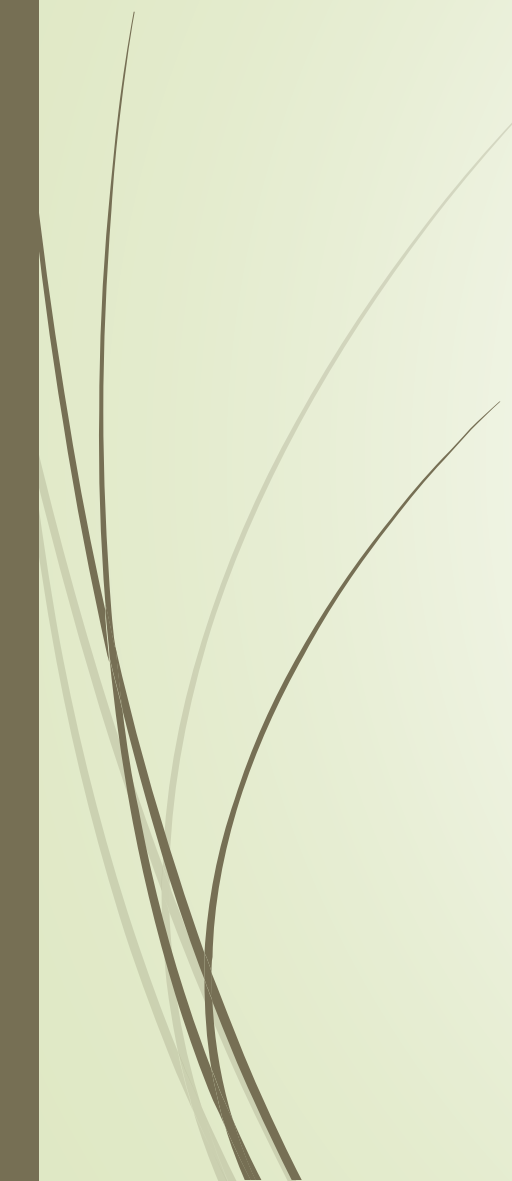


Build-Operate-Transfer (BOT) Structure (Con 'd)

- ▶ The revenues generated from the operation phase are intended to cover the followings:
 - ▶ operating costs,
 - ▶ maintenance,
 - ▶ repayment of debt principal (which represents a significant portion of development and construction costs),
 - ▶ financing costs (including interest and fees),
 - ▶ and a return for the shareholders of the special purpose company.



Shariah Compliant Securities

- Sukuk is a term mainly used for Shariah compliant securities
 - Currently many societies with majority of Muslim Population have witness Sukuk issuance
 - Based on the underlying contract in Sukuk structure, it carries different names such as:
 - Ijarah Sukuk
 - Murabaha Sukuk
 - Wakalah Sukuk
 - Istisna Sukuk
 - etc
- 



Sukuk Structuring for Project Financing

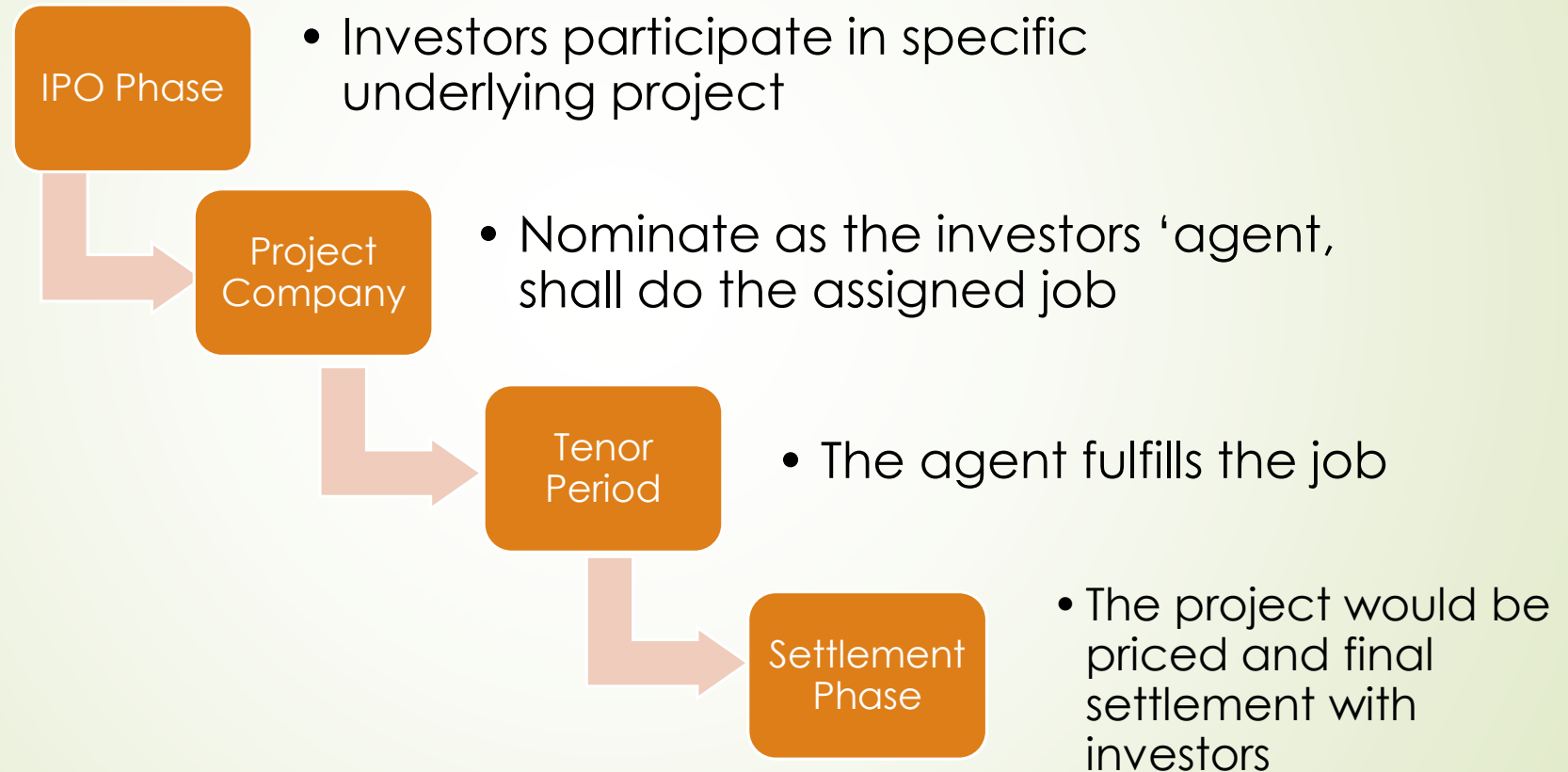
- There are different Sukuk types capable for project financing such as:
 - Musharakah Sukuk
 - Wakalah Sukuk
 - Istisna Sukuk
- Any of the above Sukuk types, carry their own advantages and disadvantages
- Musharakah and Wakalah Sukuk have variable profit rates
- Istisna Sukuk structures may have variable income or fixed income



Musharakah Sukuk Features

- Musharakah Sukuk proves Sukuk holders' participation in underlying Sukuk issuance subject
- Sukuk investors shall have ownership rights in the Sukuk underlying asset.
- As Sukuk final profit would get determined at the maturity date, Sukuk investors may received some provisional profit rates during Sukuk tenor time.
- At the maturity time, final profit/loss should be clarified and final Sukuk holders will find the settlement price.
- If Sukuk underlying asset is construction of specific project, at maturity date the underlying assets would be taken off.

Musharakah Sukuk Phases





Musharakah Sukuk Investors Reimbursement

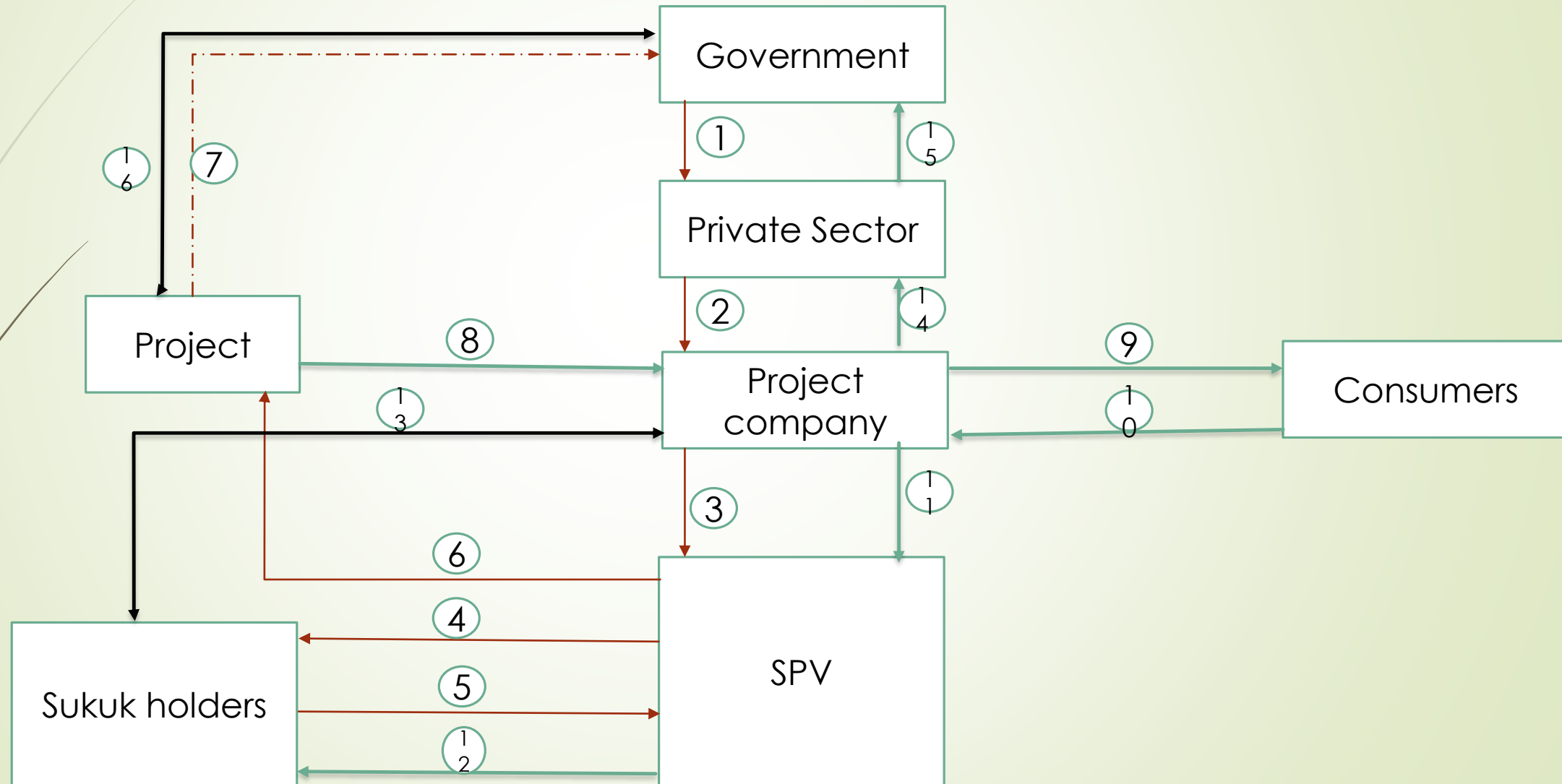
- ▶ There are different mechanisms to reimburse investors in Musharakah Sukuk which include:
 - ▶ Off taking
 - ▶ leasing
 - ▶ Financial lease
 - ▶ Operational lease
 - ▶ Product sale?
- ▶ As a result, investors may find their principal and profit at Sukuk maturity date



Musharakah Sukuk: tendency towards asset-based structure?

- ▶ Asset based Musharakah Sukuk vs. Asset backed Musharakah Sukuk
- ▶ What are the goals?
 - ▶ Moving towards strengthening asset backed structure
 - ▶ More project productivity
 - ▶ Less issuance costs
 - ▶ Strengthening off-balance sheet financing
 - ▶ More profit/loss Sharing spectrum
 - ▶ Increasing disclosure and transparency

Restructuring Musharakah Sukuk Model for project financing





Restructuring Shariah Requirements

- ▶ Assigning agency role to the company project
 - ▶ As Sukuk holders 'agent, the company may ask for some fees
 - ▶ All the received money belongs to the Sukuk holders
 - ▶ Auditing revenues is at higher importance level
- ▶ Convertibility Structure
 - ▶ Sukuk holders and project company mutual consent
 - ▶ Gharar issue in the structure
 - ▶ Determination of conversion rate
 - ▶ Determination of equity features for both parties
 - ▶ Determination of equity voting rights



Restructuring Shariah Requirements

- Usufructs Transferring
 - Usufructs affects on rents
- Financial Lease
- Operational lease
 - Determination of off taking price for the asset at the beginning
 - Determination of off taking price for the asset at maturity date

Thank you very much for your kind attention

