

THE MUSLIM COUNCIL OF BRITAIN



By email to islamic.finance@hm-treasury.x.gsi.gov.uk

Ms Aviva Rosen
Room 3/W3
Financial Services Strategy
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

26 February 2009

Dear Ms Rosen

Consultation on the legislative framework for the regulation of sukuk

I am writing with the Muslim Council of Britain's response to this consultation document.

We regard the development of Islamic finance in London as important to the overall role of London as a global centre for the financial services industry. Accordingly, it is essential to have a regulatory framework for sukuk which is clear, transparent and workable without imposing undue costs on market participants.

As a preliminary point, we regard it as fundamentally undesirable for a single term (such as "Alternative Finance Investment Bond") to have two independent statutory definitions. This would create continuing scope for confusion.

We agree with the broad regulatory goals, of defining an instrument that receives the same regulatory treatment as a conventional bond, provided that it has the economic characteristics of a conventional bond. As the FSMA 2000 regime potentially involves criminal penalties, we consider that definitions under the regulatory regime should be somewhat broader, and with less scope for difficulties of interpretation, than one encounters in the tax legislation.

Accordingly, to avoid having two meanings for the same four words, we consider that a modified version of option 1 should be adopted, with an independent regulatory definition of something called, say, an Alternative Finance Bond (AFB). As the regulatory boundaries should be stable, we hope that the definition of an AFB will be amended less often than might be the case for the tax law definition of an Alternative Finance Investment Bond (AFIB). In the remainder of this response, we expressly refer to AFBs as the issues are regulatory, not tax.

Our responses to your specific questions, using the numbering in your document, are as follows:

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1. Yes. This applies both to AFBs which have similar economic characteristics to conventional (unconvertible) debt and to AFBs which are convertible or exchangeable and which have similar economic characteristics to conventional convertible or exchangeable debt.
2. We agree that the Schedule to the Financial Services and Markets Act 2000 (Collective Investment Schemes) Order 2001, SI 2001/1062 should be amended so that AFBs are expressly excluded from being a collective investment scheme for regulatory purposes.

We also agree that the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, SI 2001/544 should be amended so that the issue of AFBs and dealing in AFBs receives the same regulatory treatment as similar transactions in conventional bonds. The draft amendments on page 25 should achieve the objective of similarity of regulatory treatment, subject to the other comments in this response.

3. We concur with option 1 conceptually, but regard it as important to use a different term, AFB, for regulatory purposes, which differs from the term AFIB which is used for tax purposes. As soon as one has two independent definitions, it becomes possible for an instrument to qualify under one definition but not the other. Use of the same term would therefore create confusion.

Once one recognises that a separate regulatory definition is being considered, the proposed definition set out on page 25 needs further consideration.

77A (2)(c) We fail to see why perpetual AFBs that pay no more than a normal commercial return should be treated less favourably for regulatory purposes than a conventional perpetual bond. A minor consequential amendment may be needed to 77A (2)(d)(i).

77A (26)(f) We see no reason why an AFB should be required to be listed, when there is no requirement for a conventional bond to be listed. This regulatory question for an AFB needs to be considered independently of the tax law issues, since we are considering independent definitions which are to be used for different purposes. By definition, an AFB will only pay “debt-type” economic returns. What regulatory arbitrage does the FSA have concerns about?

4. No.
5. No. See answer to 3 above.
6. Yes. Tax law often has very finely defined boundaries, which are often difficult to interpret. That is not appropriate for legislation with criminal sanctions.

We would be pleased to discuss these issues with you in person if that would be helpful.

Yours sincerely

Mohammed Amin
Chairman of the Business & Economics Committee

business@mcb.org.uk