



## Islamic Finance Experts Group

UK Tax Budget provisions facilitating sukuk issuance

Nash Jaffer  
14 July 2009

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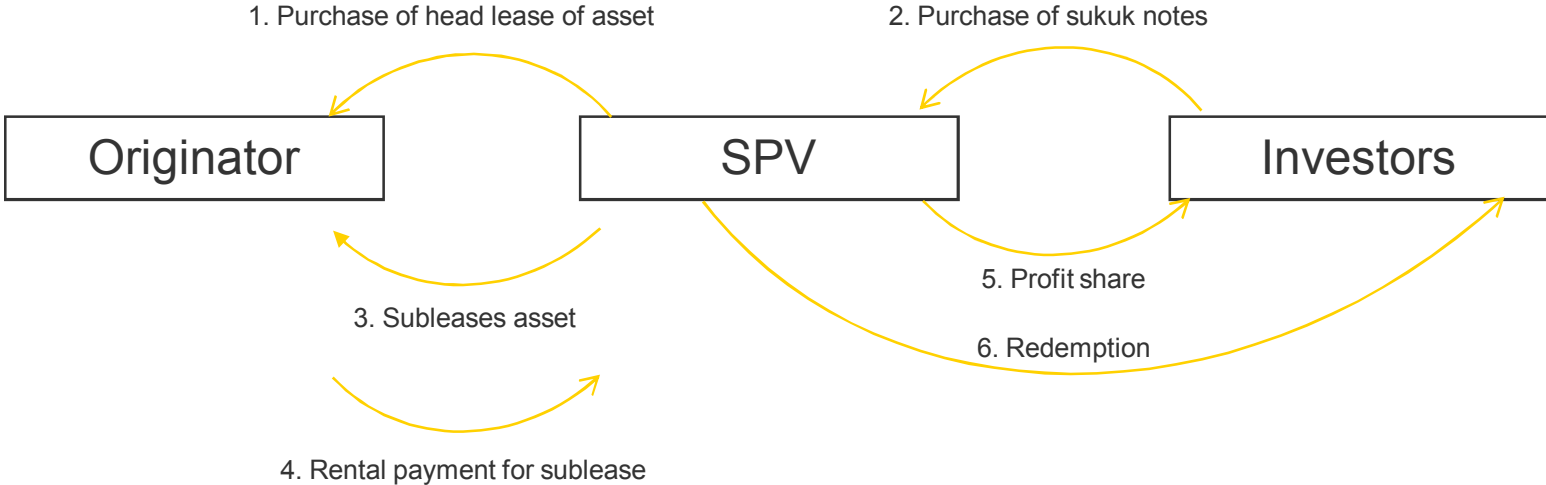
# Sukuk

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Sukuk is similar to conventional securitisations except that

- ▶ sukuk holders are part owners of the underlying asset, having financial rights to a share of the revenues generated by those assets
- ▶ the maturity of the sukuk corresponds to that of an underlying activity or project
- ▶ the underlying assets themselves must be sharia'a compliant (eg: Property etc.)
- ▶ return of capital to investors may not be guaranteed

# Sukuk al-ijara structure



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# SDLT and sukuk

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- ▶ SDLT is a charge on the acquisition of a chargeable asset and does not arise in the issuance of a conventional bond.
- ▶ The Government announced in the 2008 Budget that it would engage in consultation.
- ▶ Consultation focused on the form of relief to be provided to offset any SDLT consequences.
- ▶ Document was issued in June 2008 and EY submitted response.
- ▶ Proposed SDLT relief will remove the SDLT charge on the transfer of property to and from the SPV and ensures no charge arises on the bondholders.
- ▶ Effective date is when Finance Act 2009 receives Royal Assent.

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# Corporate Tax and sukuk

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- Legislation introduced in Finance Act 2007
- ▶ Sukuk treated as a loan relationship. Consequently, periodical payments to holders treated as interest although very detailed conditions have to be met
- ▶ Periodical payments to investors must not exceed a reasonable commercial return on an equivalent loan
- ▶ Sukuk must be listed on a recognised stock exchange
- ▶ Another barrier is that the following could all give rise to capital gains:
  - transfer of the land asset to the SPV;
  - the grant of a lease by the SPV to the originator;
  - the eventual return of the land asset
- ▶ New provisions provide relief by “ignoring” the various transactions
- ▶ Originator treated as owning the asset throughout the period of the bond
- ▶ New provisions also provide that the originator will continue to be entitled to capital allowances whilst the land asset is held by the SPV.

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# Indirect tax and sukuk

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- ▶ No specific VAT legislation introduced in regard to Islamic finance products.
- ▶ Consequently the VAT treatment of a sukuk must be determined within the current VAT regulations.
- ▶ The VAT treatment will not vary if sukuk is listed on a recognised stock exchange.
- ▶ The VAT treatment of the investor's acquisition of his interest in the sukuk will be dependent on the characteristics of the acquisition (e.g., is the interest in the form of a bond and what are the terms of the bond).
- ▶ The periodic payments to the investor may give rise to a VAT charge but again this will be dependent on the characteristics of the investors holdings in the sukuk.
- ▶ Need to consider carefully the VAT treatment of the transfer of assets to the SPV, however it is expected that this transfer will be VAT free as a transfer of a going concern.
- ▶ HMRC has initiated a process of consultation to solve the VAT anomalies.



**Thank you**

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