

More than just Dana Gas

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2018 has been another positive year for the Islamic finance industry with continued global growth including an upsurge in Islamic retail banking and Sukuk issuance activity in the UK alongside important legislative and regulatory changes in the Middle East and Asia enhancing the industry's prospects for the future. This year has also seen the impact of an impending Brexit and one of the largest litigation sagas to rock the Islamic finance industry come to an end with the successful refinancing of the infamous US\$700 million Dana Gas Sukuk.

Review of 2018

Dana Gas Sukuk

Dana Gas, the Middle East's largest regional private sector natural gas company, presented an offer to their Sukukholders to restructure the Sukuk as well as declaring that the Sukuk was no longer Shariah compliant and therefore unlawful under UAE law. The Sukukholders declined this offer sparking a major cross-jurisdictional litigation battle center in large part on the mismatch in governing law across the documentation suite for the Sukuk.

The English High Court order blocked Dana Gas from making dividend payments unless it also set aside money to redeem the Sukuk. Conversely, the Federal Court of First Instance in the Emirate of Sharjah ordered Dana Gas to suspend enforcement of the English court's ban on paying dividends. This conflict between rulings has sparked debate on whether the English court's dividend ban was indeed enforceable in the UAE — the outcome of which was not resolved. In May 2018 all parties agreed a deal to

restructure the Sukuk and legal proceedings finally came to an end across all jurisdictions. Alongside Dana Gas shareholders, an overwhelming 94% of Sukukholders approved of the refinancing.

Whilst presenting challenges for the industry as a whole, the case serves to reinforce that Sukuk can withstand legal and public scrutiny, with Sukukholders remaining invested in the company which now aims to develop its global asset portfolio. The crucial lessons to be learned include: the need for consistency in the suite of transaction documents on choice of law provisions, to clearly allocate the risk of invalidity of the Sukuk by ensuring that non-Shariah compliance is not a ground to make payment obligations void, and to ensure harmonization of cross-border judgments to bolster the enforceability of obligations.

UK — Brexit boom for the Islamic finance industry

Brexit could send the Islamic finance industry on an upward trajectory in the UK as the government looks to build economic links with the Middle East and Asia to bolster foreign direct investment including from Shariah compliant sources. In early 2018, AlRayan Bank issued the UK's first asset-backed Sukuk in the sum of GBP250 million (US\$318.69 million) (the largest ever sterling denominated Sukuk issuance), becoming the first bank in the world to issue a public Sukuk in a non-Muslim country and enhancing the UK's position as the western hub for Islamic finance.

The growth of Islamic finance is dependent in many respects on the creation of regulatory frameworks that do not prejudice Shariah compliant instruments relative to the conventional market. The UK is certainly aware of this and most recently the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2018 amended the definition of 'Alternative Finance Investment Bonds' (AFIBs) in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001. As a result, AFIBs, such as Sukuk, can trade on multilateral trading facilities and AFIBs will now be treated in the same way as conventional bonds for trading purposes; therefore providing a level playing field for Shariah compliant instruments.

Developments in Kenya and Pakistan

Another jurisdiction that has looked to improve its legislative framework is Kenya, which is set to introduce new regulations on Takaful following The Insurance (Amendment) Act 2016. The regulation is currently in draft form and the Insurance Regulatory Authority (IRA) aims to publish it in early 2019. The goal is to stimulate issuance of Sukuk, increase the Takaful offering in Kenya and help boost international investment.

On the 2nd November 2018, the Securities and Exchange Commission of Pakistan enforced the Shariah Governance Regulations 2018 which govern Shariah compliant

companies, entities and Islamic financial institutions. This is a major breakthrough as it is the first time a regulator has defined comprehensive requirements for companies that deem themselves to be Shariah compliant, rather than the popular focus taken by regulators in the Middle East and Asia on banks and insurance firms. This aims to bring standardization and transparency in Shariah compliant business practices by aligning with the Shariah standards of AAOIFI.

Preview of 2019

The global Islamic finance industry continues to flourish following the successful refinancing of the Dana Gas Sukuk and the ground-breaking UK issuance of a true asset-backed Sukuk. Islamic finance as an industry is dynamic and constantly evolving, not least from a legal perspective, with 2019 set to continue this trend. As the industry continues to adapt to the evolving political landscape and take advantage of new opportunities, such as the rise of fintech start-ups and the potential of blockchain, in particular, to limit exposure to risks on transaction security, the future looks bright.

Conclusion

To continue to grow and take market share from conventional banking, the Islamic finance industry needs to be at the forefront of anticipating legal and regulatory developments. It is a challenge which it is meeting in part but there is much work to do and 2019 will, we hope, see some significant legislative developments helping to push the industry ever forward.

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