

Optimization of Sukuk to Support Sustainable Development in Indonesia

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ABSTRACT

Sukuk is now globally known as one of the fast-developing financial instruments that consistently apply Islamic principles. The role of Sukuk in Indonesia is not limited to the development and expansion of a Sharia-based economy. It also plays a larger role in the financing of both public and private projects. The matter regarding the issuance of Sukuk is still under debate, especially as it pertains to the beneficial ownership of an underlying asset within the law of ownership. This research also uses Sharia's perspective to determine whether the blending of *Akad Wakalah* (Proxy Agreement) and *Akad Ijarah* (Sale and Purchase Agreement) in one transaction is allowed under Sharia law. The research will hopefully offer a clear approach to legal certainty while fulfilling the requirements of Sharia law. Its focus will be on the regulation and practical application of Sukuk and the need for its legal certainty and development in society. Questions regarding the validity of beneficial ownership upon assets as the underlying asset of Sukuk, in addition to the validity of *Akad Wakalah* and *Akad Ijarah* as simultaneously used in a single transaction, will be answered.

Keywords: *Sukuk, beneficial ownership, Akad Wakalah, Akad Ijarah*

1. INTRODUCTION

In the 1970s, an economic system based on Islamic concepts was proposed by Sharia experts in the Middle East.¹ It was inspired by the spirit of Sharia, which aims for a bigger, nobler purpose, namely the manifestation of an entirely prosperous society.

An economic system based on Sharia law, in essence, prioritises a just system that features profit-sharing but forbids all attempts on usury. The system slowly but surely has shown early satisfying results, which can be seen not only in Middle Eastern/Islamic countries but also in other parts of the world where Islam is not the major religion. One indicator is the rapid growth of economic institutions that partially or entirely implement Sharia law in their daily management². The key instrument that has been the backbone of Sharia law implementation in economic systems is Sukuk, or as it is known in some parts of the world, Sharia Bonds. As a country with the world's largest Islamic community, Indonesia seeks the opportunity to infiltrate and, as soon as possible, dominate this economic

sector. Therefore, the Government of the Republic of Indonesia ('GoI') has already initiated and regulated the issuance of Sukuk with Regulation Number 19 the Year 2008 regarding *Surat Berharga Syariah Negara* (Sovereign Sukuk). The sole purpose of this regulation is to facilitate the issuance of Sukuk and provide legal certainty for transactions. For GoI, Sukuk will be an instrument that provides financing for the general expenditure of GoI or several of GoI's projects. The regulation also constitutes a bold statement about the current propagation of Sharia law in Indonesia, especially in the strategic sector.

In essence, Islamic law is not just limited to the management of relations between the Creator and His creatures but also between the creatures themselves, not least humans. For financial transactions, Islam has ruled that all such negotiations must rely on 'Akad' (contract), whether they refer to 'Sale and Purchase Akad' or 'Profit-sharing Akad'.³ 'haram' (forbidden) is popular among transactions that following Sharia law. Interest in economic terms is *haram* for all kinds of modification. This can be confusing for practitioners of Sharia economics, since almost every configuration in conventional economic systems has been carefully

¹ Mat Ismail and Ismail Yusof, *A Review of Fiqh al-Mua'malat Subjects in Economics and Related Programs at International Islamic University Malaysia and University of Brunei Darussalam*, (Januari, 2015).

² Cihak Martin and Hesse Haiko, *Islamic Banks and Financial Stability: An Empirical Analysis*, IMF Working Paper.

³ Zainul Arifin, *Dasar-Dasar Manajemen Bank Syariah* (Jakarta: Rennaian, 2005), page 36-37.

considered as *haram*, or illegitimate, under Sharia law. To counter such confusion, Sharia law has created alternatives for collecting and spending money. Those alternatives are *akad musyarakah*, *akad mudharabah*, a mixture of *akad syirkah* and *akad ijarah*, *akad salam* and *akad istishna*.⁴ For the sake of financing, GoI has issued several Sovereign Sukuks to facilitate financing that mainly relies on Islamic law. Those *Akads* are mainly applicable for simple, two-party transactions. For wider applications that involve more parties, a deeper study is required to prevent and answer confusion among practitioners.

From the perspective of the application, Sukuk remains unclear in several parts of the implementation. The main role that this paper wants to highlight is that of the Investor, or in terms of Sukuk, 'Sukuk Holders' ('the Holders'). At the earlier development of Sukuk, experts in this sector claimed it was a different instrument compared to bonds. The difference can be spotted via several factors, including, but not limited to, usage of an underlying asset, possession of the underlying asset by the Holders, and the participation of the Holders in the management of the underlying asset. Usage of underlying assets was claimed to be a bold differentiation between Sukuk and conventional bonds. Thus, for several parties involved in a transaction, their legal rights and obligations concerning the underlying asset remain uncertain. It is the main purpose of this paper to seek and correctly identify the relationships between the Holders with the underlying asset, along with their legal rights and obligations.

2. FORMULATION

2.1. Formulation of the Problem

Firstly, the main purpose of this paper is to identify the remaining questions regarding the use of the underlying asset. Without knowing certainly the usage of the underlying asset and how it is managed, the Holders will remain in doubt as to how to categorise their involvement in this transaction, other than acting as an investor who bets their money on financial instruments.

Secondly, the confusion remains concerning the relationship between the Holders and the underlying asset. The underlying asset should be the key factor that differentiates between Sharia law-complied instrument and other instruments. However, that idea still remains theoretical since the underlying asset plays a minor role in the transaction of Sukuk, especially in the creation of profits to be distributed as a dividend. The Holders should be allowed to see important information regarding the underlying asset.

⁴ Muhammad Ayub, *Understanding Islamic Finance: A-Z Keuangan Syariah [Understanding Islamic Finance]*, translated by Aditya Wisnu Pribadi (Jakarta: PT Gramedia Pustaka Utama, 2009), page 76.

3.1 Purpose of the Research

There are two main purposes of this research: to provide proper information regarding the underlying asset and study the relations between the underlying asset and the Holders.

3. SUKUK AND ASSET SECURITISATIONS

In this part, Sukuk will be identified comprehensively from the fundamental principle. To understand Sukuk means identifying its complete legal standing and comparing this instrument with another similar instrument, such as conventional bonds. After that, the spotlight will be directed at enlightening the veil that hides several details regarding the process of asset securitisation. The discussion will be presented with factual examples, which is a Sovereign Retail Sukuk SR-011 Series.

3.1. The Prior Understanding of Sukuk

The term 'Sukuk' is derived from the Arabic word 'sakk', meaning document or certificate.⁵ The definition of Sukuk is understood differently in different parts of the world. One of the key players in the Sharia economic system is the *Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)*, based in Bahrain. AAOIFI defines Sukuk in its Sharia Standards, as described below:

*Investment Sukuk is certificates of equal value representing undivided shares in ownership of tangible assets, usufructs, and services or (in the ownership of) the assets of particular projects or special investment activity. However, this is true after receipt of the value of the Sukuk, the closing of the subscription and the employment of funds received for the purpose for which the Sukuk are issued.*⁶

Another expert defined Sukuk as:

*They [Sukuk] are investment certificates with both bond and stock-like features issued to finance trade or the production of tangible assets.*⁷

Sukuk plays an important role as a financial instrument that pools investment funds in several productive sectors. Sukuk is commonly mistaken for conventional bonds, given that both of them have maturity dates and pay routine dividends to their Holders until then. Sukuk Holders might be responsible for asset-related expenses, and the sale of Sukuk results in the sale of a share of an asset. In contrast, Bonds are pure debt obligations issued to finance any activity. To identify the price or value of

⁵ Sharia Financing Directory, *Surat Berharga Syariah Negara (Sukuk Negara) Instrumen Berbasis Syariah* (Jakarta: Departmen Keuangan Republik Indonesia-Direktorat Pembiayaan Syariah, Juni, 2015), page 8.

⁶ Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), *Sharia Standards*, (2015), page. 468.

⁷ Christophe J. Godlewski, Rima Turk-Ariss, and Laurent Weill, "Sukuk vs conventional bonds: A stock market perspective", *Journal of Comparative Economics* (Vol. 41 No. 3) (2013), page 137.

Sukuk, it is essential to know the creditworthiness of the issuer and the market value of the underlying asset. Thus, the underlying asset plays an undisputed role, and the ups and downs of its value can determine how much profit will be paid to the Holders.

While the underlying asset plays a big role in a Sukuk transaction, the issuer is obliged to provide proper information regarding it. The issuer must invite an independent evaluator to determine the value of the asset and provide legally recognised documents that state legally approved possession of the asset.

Sukuk investments represent a distinct class of securities issued by sovereign and corporate entities. In this paper, the discussion about corporate entities will be waived; the sole topic of discussions will be about Sovereign Sukuk. In the issuance of Sovereign Sukuk, an underlying asset is required. The Sukuk is, in essence, security which signifies ownership of an asset on which the Sukuk is issued. The existence of the underlying asset functions as a real transaction and connects the financial assets and real assets. Based on its *akad*, Sovereign Sukuk can be subject to several modifications, such as⁸

Sukuk Ijarah, based on *Ijarah Akad*;

Sukuk Mudharabah, based on *Mudarabah Akad*;

Sukuk Musyarakah, based on *Musyarakah Akad*;

Sukuk Istisna';

Another modification of Sukuk, which can be a combination of the above-mentioned *Akad*.

Until today, GoI has issued several products, which are mentioned below.⁹

Retail Sukuk;

Islamic Fixed-rate Sukuk

Surat Perbendaharaan Negara Syariah;

Hajj Investment Fund Sukuk;

Project-based Sukuk;

Foreign Exchange Sukuk;

Sukuk as Savings.

In general, the purpose of issuing Sukuk is to meet the needs of general financing or specific project financing. Sukuk provides the government and corporations with access to a source of alternative funding sources. Following the Sharia principle, all of the funds gathered from the issuance of Sukuk may only be used for

⁸ Indonesia, *Regulations about Surat Berharga Syariah Negara, Regulations Number 19 the Year 2008*, Article 3.

⁹ Wurjanto Nopijantoro, "Surat Berharga Syariah Negara *Project Based Sukuk* (SBSN PBS): Sebuah Instrumen Alternatif Partisipasi Dalam Pembiayaan Infrastruktur". *Substansi Volume 1 Nomor 2*, (2017), page. 394.

activities that comply with Sharia law. In general, Sukuk proceeds can be used for the following purposes.¹⁰

General Financing

Funds from the issuance of Sukuk that are intended for general financing are forbidden to be used to finance a particular project. The funds may be included in the overall expenditure or the current year's GoI budget. These funds will be used to finance various necessary expenses.

Project Financing

Funds from the issuance of Sukuk may be aimed to finance a specific investment activity or project. This type of Sukuk is widely known as Project Financing Sukuk. The underlying asset is a GoI project, whether it is pre-assigned to be fully funded from Sukuk issuance, or an ongoing project begun prior to the issuance of Sukuk. Consistency is a key and using the funds outside the project is forbidden.

The issuance of Sovereign Sukuk has many benefits for the country. These may include:

Adds more allowance for the State Budget

In line with the limited carrying capacity of the State Budget to initiate and drive economic sector development in a sustainable manner, Sovereign Sukuk can be optimised to allow new sources of allowance.

Finances GoI projects

Project financing through the issuance of Sovereign Sukuk is expected to be a driving force in achieving the national development goals. The issuance of SBSN is an effective and efficient alternative source of State Budget financing. In addition, project financing with Sovereign Sukuk can also increase the independence of the nation in carrying out national development, because fellow Indonesians can directly participate in the financing of the GoI projects through the purchase of Sovereign Sukuk.

Optimises the usage of State-owned Property

Issuance of Sovereign Sukuk that uses underlying assets in the form of State-owned Property can further increase the orderly administration of State-owned Property management, and be able to optimise the

¹⁰ Direktorat Pembiayaan Syariah, *Surat Berharga Syariah Negara (Sukuk Negara) Instrumen Berbasis Syariah* (Jakarta: Departemen Keuangan Republik Indonesia-Direktorat Pembiayaan Syariah, June 2015), page. 31.

potential of State-owned Property as the basis for the issuance of Sovereign Sukuk.

Boosts the development of the Sharia sector in Indonesia

The issuance of State Sukuk is expected to meet investment portfolio needs of Sharia financial institutions including Sharia banking, Sharia mutual funds and Sharia insurance. The increasing number of financial instruments based on Sharia principles is expected to encourage the growth of domestic Sharia financial institutions.

Strengthens and improve the role of Sharia economics

Through the issuance of State Sukuk, it is hoped that the Islamic financial industry can play an active role in financing the State Budget both directly and indirectly.

Creates a strong benchmark for the Sharia economic system

The issuance of State Sukuk is expected to become a benchmark for other Sukuk issuances, both by corporations and other entities, such as regional governments.

Reaches a wider scope of investor

With its flexibility, Sovereign Sukuk can further expand the basis of investors because it is not only limited to reach Sharia-compliant investors but also conventional investors.

3.2. Retail Sovereign Sukuk SR-011 Series.

Retail Sovereign Sukuk SR-011 Series is one of the modifications on Sovereign Sukuk issued by GoI on 28th March 2019. The *Akad* used in this Sukuk is *Ijarah Akad* with the *Asset to Be Leased* scheme. As a Retail Sukuk, this product is sold in the secondary market and issued exclusively for individual investors. The issuance of SNR-011 is based on *Ijarah* Objects, which are ongoing projects listed in the State Budget Year 2019 and state assets in the form of land or buildings that have been approved by the Minister of Finance.

The governing laws which have been applied to manage this arrangement are divided into several regulations. Here are some of them starting from the higher-level regulations to the lower regulations:

Government Regulation Number 56 the Year 2008 about *Perusahaan Penerbit Surat Berharga Syariah Negara*, in which this specific regulation had been officially changed to Government Regulation Number 73 the Year 2012 about *Perubahan Atas Peraturan Pemerintah Nomor 56 Tahun 2008 tentang Perusahaan Penerbit Surat Berharga Syariah Negara*.

Government Regulation Number 57 the Year 2008 about *Pendirian Perusahaan Penerbit Surat Berharga Syariah Negara Indonesia* in which this specific regulation had been officially changed into Government Regulation

Number 127 the Year 2015 about *Perubahan Atas Peraturan Pemerintah Nomor 57 Tahun 2008 tentang Pendirian Perusahaan Penerbit Surat Berharga Syariah Negara Indonesia*.

Minister of Finance Regulations Number 129/PMK.08/2011 about *Penggunaan Proyek Sebagai Dasar Penerbitan Surat Berharga Syariah Negara*.

Minister of Finance Regulations Number 205/PMK.08/2017 about *Penggunaan Barang Milik Negara Sebagai Dasar Penerbitan Surat Berharga Syariah Negara*.

Minister of Finance Decision Number 215/PMK.08/2008 about *Penunjukkan Bank Indonesia Sebagai Agen Penata Usaha, Agen Pembayar, dan Agen Lelang Surat Berharga Syariah Negara di Pasar Dalam Negeri*.¹¹

At the time this product was issued, several legal documents supported the issuance of Sukuk for the sake of guaranteeing legal certainty. Those documents are tied in a memorandum, because they codify every step of transactions and movement of funds from one party to another. Before mentioning those documents, it is essential to understand the movement and management of funds, as well as the break down of all the parts that support the movement of funds. Below is attached the image that portrays the whole construction:

To explain the process of issuing this product, several steps are required to realise profit-sharing. The transaction is divided into three different steps: Issuance of Sovereign Sukuk, Profit-Sharing and Maturity Date. For the issuance, the GoI first orders *Ijarah* Objects to be used as the underlying asset once the Sukuk has been issued. The objects must meet several criteria provided by the SPV assigned to manage the transaction. Then, a *Wakalah* Agreement is signed that will transfer the rights to manage the project to the GoI. The rights are limited to the issuance of Sukuk. At the same time as the *Wakalah* Agreement is signed, a *Ba'I* Agreement is also signed to switch the beneficial ownership of the land/buildings classified as State-owned properties. In the future, that must be used to issue a Sukuk.

Part two of the transaction is profit-sharing. The profit-sharing process is completed by signing the *Ijarah Asset to be Leased Akad* (rent agreement) between GoI and SPV. The *ujrah*, or rent money, is then given by the GoI to SPV and further transferred to the Holders.

The last part of the process is the steps taken upon the maturity date. It is essential for the SPV to sell back the State-owned Property to the GoI as it is obliged

¹¹ Kementerian Keuangan, *Memorandum Informasi Sukuk Negara SR-011 Dalam Mata Uang Rupiah Dengan Akad Ijarah Asset to be Leased*, (Memorandum Informasi was accessed on <https://www.kemenkeu.go.id/media/11989/memo-info-sr-011-final-sent.pdf>).

by Regulations Number 1 the Year 2004 about *Perbendaharaan Negara* and Regulations about Sovereign Sukuk. Any remaining rent money that has not been paid by the GoI must be paid off at the re-transfer of assets.

All of the processes in that transaction must be supported with several legal documents, including:

1. Official Letter from GoI to order *Ijarah* Object from the SPV;
2. *Wakalah Akad* (Agreement) that gives the GoI the right to:
 - a. Procure, provide, and give *Ijarah Objects* in the form of a project with specific requirements;
 - b. Build, finish up, and transfer the project with full responsibilities within the pre-agreed time;
 - c. Use the gathered funds from the issuance of Sukuk to procure, provide, and transfer the project;
 - d. Administer the project on behalf of SPV until the maturity date;
3. Sale and Purchase Agreement (*Ba'I Akad*);
- Rent Agreement (*Ijarah Asset to be Leased Akad*);
4. Maintenance of *Ijarah* Object Agreement;
5. Statement to Sale from the SPV;
6. Statement to Buy from the SPV.

All of the documents must be reviewed by both parties; compliance with higher governing laws is obliged. This is an essential part of the transactions because the transaction involves State-owned Property. Said property is tightly regulated. The distinctive difference from other types of property is that the State-owned Property is forbidden to be sold in any kind of way, except by transfer of beneficial ownership.

3. SUMMARY AND CONCLUSION

This article has attempted to provide some background for understanding how the law—particularly its enforcement—governs the issuance of Sukuk and how it affects the development of the Islamic capital market and general ecosystem. From the explanation above, it is clear that underlying assets play a major role in the issuance of Sukuk. All constructions stemmed from the issuance of Sukuk depend on how the underlying asset is determined.

The Holder is the beneficial owner of the underlying asset. In Indonesia, the full transfer of an asset is forbidden, but beneficial ownership transfer is allowed for State-owned properties.

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