

ISLAMIC CAPITAL MARKET IN MALDIVES: A REFORM-ORIENTED ANALYSIS

Mohamed Shujau*

Rusni Hassan**

Syarah Syahira Mohd Yusoff***

Aishath Muneeza****

ABSTRACT

This study analyses legal and regulatory framework of Islamic capital market (ICM) in the Maldives to find out the legal reform required to further develop ICM in the country. The regulatory authority for ICM in the Maldives is the Capital Market Development Authority which has set up an apex Shari'ah Advisory Council to seek advice on Shari'ah related matters and has enacted the regulations required for ICM. This study adopts doctrinal legal research and qualitative study using the content analysis approach. It is imperative to note that only limited research has been found on the subject and as such, it is anticipated that findings of this research will assist the policymakers to understand the legal reform required to further strengthen ICM in the Maldives. Findings of this study reveal that there is a need to amend the Securities Act (2006) to recognize Shari'ah Advisory Council for capital markets as a statutory body. The findings suggest the Shari'ah Advisory Council to make their decision binding, and the regulations enacted for ICM need to be amended considering the existing hiccups and challenges faced.

Keywords: Islamic Capital Market, The Maldives, Legal Framework, Reform.

* Lecturer, Islamic University of Maldives. Email: mohamed.shujau@ium.edu.my.

** Professor, IIUM Institute of Islamic Banking and Finance, International Islamic University Malaysia. Email: hrusni@iiu.edu.my.

*** Assistant Professor, IIUM Institute of Islamic Banking and Finance, International Islamic University Malaysia. Email: syarahyusoff@iiu.edu.my.

**** Associate Professor, INCEIF University. Email: muneeza@inceif.org

PASARAN MODAL ISLAM DI MALDIVES: ANALISIS BERORIENTASI PEMBAHARUAN

ABSTRAK

Kajian ini menganalisa rangka kerja perundangan dan kawal selia pasaran modal Islam (ICM) di Maldives untuk mengetahui pembaharuan undang-undang yang diperlukan untuk membangunkan lagi ICM di negara ini. Pihak berkuasa kawal selia untuk ICM di Maldives ialah Pihak Berkuasa Pembangunan Pasaran Modal yang telah menubuhkan Majlis Penasihat Syariah tertinggi untuk mendapatkan nasihat mengenai perkara berkaitan Syariah dan telah menggubal peraturan yang diperlukan untuk ICM. Kajian ini menggunakan penyelidikan perundangan doktrinal dan kajian kualitatif menggunakan pendekatan analisis kandungan. Adalah penting untuk dinyatakan bahawa penyelidikan mengenai subjek ini adalah terhad dan oleh itu, adalah dijangkakan bahawa penemuan penyelidikan ini akan membantu penggubal dasar memahami pembaharuan undang-undang yang diperlukan untuk mengukuhkan lagi ICM di Maldives. Dapatan kajian ini mendedahkan bahawa terdapat keperluan untuk meminda Akta Sekuriti (2006) untuk mengiktiraf Majlis Penasihat Syariah bagi pasaran modal sebagai badan berkanun dan untuk menjadikan keputusan mereka sebagai peraturan yang mengikat. Dapatan mencadangkan keperluan untuk meminda peraturan berkaitan ICM dengan mengambil kira kekurangan dan cabaran yang dihadapi.

Kata Kunci: Pasaran Modal Islam, Maldives, Kerangka Perundangan, Pembaharuan

INTRODUCTION

The Maldives is a small island nation with a hundred percent Muslim population.¹ According to Article 10 of the Constitution of the Maldives, Islam is the religion of the state and it shall be the basis to make all the laws of the country. Further, it is also stated that all laws enacted in the country shall be consistent with Islamic law.² Despite this, *riba* (usury) based economic and financial system is still on-going and it is only in 2003 that the first form of Islamic finance which is *takaful* (Islamic insurance) was offered in the country by Amana Takaful Maldives (ATM). The ATM started its operation under a conventional insurance license and still remains in the operation under the same conventional insurance license which it obtained then. This is because up until now, the central bank of the country, Maldives Monetary Authority (MMA) does not differentiate between *takaful* and conventional insurance. As such, it would not be wrong to state that the official license for an Islamic financial institution to operate was given by MMA to Maldives Islamic Bank Plc (MIB) which commenced its operations in 2011 and its operations were regulated under the Islamic Banking Regulation 2011.

In the Maldives, the Islamic capital market (ICM) is regulated by the Capital Market Development Authority (CMDA) which is a statutory body established under the Maldives Securities Act (2006).³ According to section 4 of the Act, there are four primary objectives of establishing CMDA and they are: to create securities market with primary and secondary market; to protect the rights of investors who invest in securities; to regulate and supervise the securities market; and to prevent misconduct in the securities market and to maintain the confidence of the investors in the securities market. Section 62 of the Act defines securities as: debentures, bills or bonds issued or proposed to be issued by the government; debentures, stocks, shares, bonds or notes issued or proposed to be issued or any right warrant or option in

¹ Ismail Wisham and Aishath Muneeza, "Harmonization of Civil Law and Shariah in a Small Island Nation: The Republic of Maldives Case Study," *Journal of Alternative Perspectives in the Social Sciences* 3, no.1 (2011): 208-239.

² See: Article 10 Maldives' Constitution of 2008

³ See: Section 3 Maldives Securities Act No. 02/06 (amendments) 2016.

respect thereof by a body corporate or any other institution; any other instruments as CMDA may prescribe to be securities for the purposes of this Act.⁴

To establish the ICM, one of the first steps taken by the CMDA was to use the power granted to CMDA in the above section to prescribe any instruments it deems as a security and to include Islamic securities within the definition of securities in June 2011 via a circular.⁵ In the same year, an apex Shari'ah Advisory Committee (now known as Shari'ah Advisory Council) was formed to provide advice on Shari'ah related matters required for the ICM activities by the Board of Directors of CMDA.⁶ In 2001, the CMDA identified three main challenges facing the development of ICM in the Maldives and they are: legal challenges where it was observed that the required legal framework for the development of ICM is missing in the country; lack of awareness of the stakeholders about the basics of Islamic finance; and lack of trained human resources.⁷

Despite the numerous challenges faced, the CMDA has successfully created the ICM in the Maldives. Nevertheless, while the CMDA has managed to bring the ICM into the next level, it is imperative to conduct a research to find out the challenges faced and to recommend ways to overcome those challenges. Until now, only limited research has been available on the matter. For instance, Aishath Muneeza has presented a case study on the development of ICM within the limited Islamic finance services in the Maldives, and has identified several key challenges faced. These are: lack of awareness among the industry players; limited number of players in the market; absence of liquidity in the secondary market; Shari'ah governance challenges;

⁴ Section 62 Maldives Securities Act No. 02/06 (amendments) 2016.

⁵ "Inclusion of 'Islamic Securities' in the Definition of 'Securities'," Circular No. (IUL) 179-3.1 /1/2011/45, Capital Market Development Authority, 2011.

⁶ "Islamic Capital Market Quarterly Bulletin," Capital Market Development Authority, accessed June 3, 2022, <https://cmda.gov.mv/assets/CMDA-ICM-Reports/CMDA-3rd-Quarter-2011-English.pdf>.

⁷ *Ibid.*

absence of incentives; and presence of legal inhibitions for the growth of Islamic finance.⁸

Therefore, the objectives of this paper are to analyse legal and regulatory framework of ICM in the Maldives, and to find out the legal reform required to further develop ICM in the country. Since no research has been conducted exclusively on the ICM's legal framework of the Maldives, this present research is therefore timely.⁹

This paper is divided into six sections. Followed by this introduction, section two discusses the legal and regulatory framework of ICM in the Maldives followed by section three which presents the methodology. Section four presents the legal challenges while section five discusses the reforms required to further develop ICM in the Maldives followed by the conclusion. It is anticipated that the findings of this research will assist the policymakers to understand the legal reform required to further strengthen the ICM in the Maldives.

LEGAL AND REGULATORY FRAMEWORK FOR ICM IN THE MALDIVES

In the Maldives, the regulatory authority for ICM is the CMDA which has the authority under section 60 of the Maldives Securities Act (2006) to issue regulations to regulate the matters related to ICM. Currently there are four main regulations exclusively governing Islamic securities and related matters.

They are: Regulation on Islamic Securities Screening (2013); Regulation on Sukuk Issuance (2013); Regulation on Registration of Shari'ah Adviser (2013); and Regulation on Capital Market Shari'ah Advisory Council (2013). Overview of these four Regulations is provided in Table 1 (below). In addition to these Regulations, there are

⁸ *Ibid.*

⁹ However, there are numerous research found on the viability of Islamic banking and finance by studying the legal and governance framework of different countries. Example see: Moegamat Igshaan Taliep, Rusni Hassan, and Adnan Yusoff, "Viability of Islamic Banking and Finance in South Africa: A Look at The Legal Framework and Governance," *IJUM Law Journal* 18, no.2 (2012): 239-260.

certain regulations such as the Continuing Disclosures and Obligations of Issuers (2019) which is applicable to both conventional and Islamic capital markets.

Table 1: Summary of regulations exclusively covering ICM matters in the Maldives

Regulations	Details
Regulation on Islamic Securities Screening (2013)	This regulation provides the Shari'ah screening criteria adopted in the country for listed companies who intend to offer Shari'ah compliant shares. According to this regulation, there are three stages involved in Shari'ah screening which is: qualitative screening where activities in the prohibited list shall not be the core business or a substantial part of the business of the company to qualify the company to go to the next stage of screening; quantitative screening of the company where it is checked that the revenue generated from business which consists any of the activities listed in the prohibited list of activities-, does not exceed 5 per cent of the total revenue of the company; the total amount of interest bearing debts of the company does not exceed 33 per cent of the total tangible assets; and the total amount of interest bearing receivables does not exceed 33 per cent of the total assets; and the stage is purification stage where if any there is any tainted income of the company revealed, that tainted income portion shall be purified by

	giving to charity. The screening of the companies will be conducted semi-annually.
Regulation on Sukuk Issuance (2013)	This regulation provides for the significant Shari'ah conditions and the regulatory requirements that must be observed in the issuance of sukuk in Maldives where it is a requirement to have a registered Shari'ah Adviser at CMDA to structure the sukuk. The sukuks which are defined in the regulations are: <i>ijarah sukuk</i> ; <i>Mudarabah sukuk</i> ; <i>Musharakah sukuk</i> ; and <i>Murabahah sukuk</i> .
Regulation on Registration of Shari'ah Adviser (2013)	This regulation sets the requirements that needs to be fulfilled by a Shari'ah Adviser who intends to advice in ICM who needs to be registered with CMDA. The qualification, competency and the procedure are laid down in this regulation. Currently there are only two registered Shari'ah Adviser in the country. ¹⁰

¹⁰ "Sharia Adviser Registration," Capital Market Development Authority, accessed June 3, 2022, https://beta.cmda.gov.mv/en/registries?registry_type=20.

Regulation on Capital Market Shari'ah Advisory Council (2013)	This regulation provides the details related to the establishment, qualification, competency and procedures related Capital Market Shari'ah Advisory Council.
---	---

Source: Author's own (compiled and summarized from the respective regulations)

It is imperative to note that other than the above stated Regulations, there are other general laws of the country related to commercial transactions which are also applied to ICM such as laws related to companies, tax and land.¹¹ There are some legal challenges presented in some of these laws as well. For instance, section 18(e) of the Land Act¹² states that if any dwelling or land is being sold, then 15% of the purchase price of the dwelling or the land shall be paid to the government as tax. Section 18(d) states that the purchaser of the dwelling must be a Maldivian citizen. In conducting *Muarabahah* transactions, these provisions of the land law could inhibit the growth of Islamic finance as double taxation on the land transfers conducted in the *Murabahah* transaction will occur and foreign financial institutions and foreigners will not be able to buy the land or even to conclude the *Murabahah* transaction.¹³

In the Maldives, currently there are 14 institutions dealing with Islamic financial services and the details of these entities are provided in Table 2 (below). Since there is no official data disclosed by any of the government entities nor by the regulatory authorities about the

¹¹ Simmons and Simmons, "Report on Developing a Sukuk Market in the Republic of the Maldives (Summary Report-2013)," Capital Market Development Authority, March 9, 2022, [https://beta.cmda.gov.mv/en/publications/report-on-developing-a-sukuk-market](https://beta.cmda.gov.mv/en/publications/report-on-developing-a-sukuk-market;); "Developing a Sukuk Market in the Maldives," 2011, <https://www.cmda.gov.mv/assets/Consultancy-Reports/Sukuk-Market-Final-Report-SiiA.pdf>.

¹² Maldivian Land Act. <https://www.mvlaw.gov.mv/pdf/translation/Land.pdf>

¹³ "Developing a Sukuk Market in the Maldives," 2011, <https://www.cmda.gov.mv/assets/Consultancy-Reports/Sukuk-Market-Final-Report-SiiA.pdf>.

developments of Islamic finance in the country, it is not easy to state the growth and asset size of it.

Table 2: Institutions Providing Islamic Financial Services in the Maldives

No.	Name of the Institution	Contribution	Year of Establishment
1.	Amana Takaful Maldives	First Takaful Operator	2003
2.	Maldives Pension Administration Office	Pensioners got the opportunity to invest their money in Shari'ah compliant products and services.	2009
3.	Maldives Islamic Bank	First full-fledged Islamic bank	2011
4.	HDFC Amna	First Islamic house financier	2012
5.	Alia Investment Maldives	First private corporation providing Shari'ah compliant vehicle finance	2013
6.	Maldives Hajj Corporation	National Hajj pilgrimage fund	2013

7.	Ayady Takaful	First Takaful Window of Allied Insurance	2014
8.	Bank of Maldives Islamic	First Shari'ah-compliant Banking and finance services window	2015
9	Maldives Transport and Contracting Company	Started offering Shari'ah compliant finance facility in engine purchasing	2015
10.	Housing Development Corporation	A government corporation offering Islamic house finance facility	2016
11.	Litus Automobiles	A private company offering Islamic vehicle finance facility	2016
12.	Maldives Centre for Islamic Finance	An institution established by the government for promoting Maldives as Islamic finance hub in South Asia.	2016
13.	Hazana Maldives	A 100% government company created to act as a SPV	2016
14.	SME Development	A specialized financial institution providing financial products and ancillary services to Micro, Small and Medium Enterprises	2022

	Finance Corporation ¹⁴	(MSMEs) and entrepreneurial start-ups with the primary purpose of easing access to finance for MSMEs who announced to start Islamic finance operations in 2022.	
--	-----------------------------------	---	--

Source: Compiled from Aishath Muneeza (2018)¹⁵, Maldives Center for Islamic Finance and Refinitiv (2018)¹⁶ and Aishath Muneeza (2022)¹⁷

In the Maldives, there are a total of 10 listed companies including two companies offering Shari’ah compliant equities, and a company that issued sukuk. The two companies offering Shari’ah compliant equities are the ATM and MIB. Whereas the company that had offered sukuk for four times is Housing Development Finance Corporation (HDFC) which offered the *Mudarabah* sukuk in year 2013, 2017, 2019 and 2020. It is important to highlight that in the Maldives, the corporate sukuk structure implemented does not have any involvement of a special purpose vehicle (SPV) as currently there is no law to regulate the establishment and regulation of SPV.

RESEARCH METHODOLOGY

¹⁵ Aishath Muneeza, “Establishment of Islamic Capital Market in Jurisdictions with Limited Islamic Financial Services: Case Study of Maldives,” *International Journal of Law and Management* 60, no.2 (2018): 373–385.

¹⁶ “Maldives Center for Islamic Finance Limited Financial Year 2018,” Auditor General Office, June 24, 2019, <http://www.audit.gov.mv/Uploads/AuditReports/2019/06June/Maldives%20Center%20for%20Islamic%20Finance%20Limited%20Audit%20Report%20Financial%20Year%202018.pdf>.

¹⁷ Aishath Muneeza, “SME Development Finance Corporation of the Maldives Launches Islamic Window,” *Islamic Finance News*, April 21, 2022, <https://www.islamicfinancenews.com/sme-development-finance-corporation-of-the-maldives-launches-islamic-window.html>.

This research adopts doctrinal legal research which is a qualitative study using the content analysis approach. The primary data is collected mainly from the legislations and regulations applied in the Maldives' ICM and via unstructured interviews conducted with experts working in the Islamic finance industry of the Maldives.

To protect the interest of the informants, it has been agreed prior to the interview that their details and profiles shall remain anonymous. Additionally, the secondary data is gathered from academic articles from various academic journals, relevant reports and also relevant websites. These resources are analyzed critically to derive conclusions.

LEGAL CHALLENGES AND REFORMS REQUIRED FOR ICM IN THE MALDIVES

There are two main types of legal challenges facing the development of ICM in the Maldives and they are: issues found in the existing laws as well as the lack of laws to develop the ICM. As such, it is imperative to understand these challenges before proposing the reforms required to take the ICM to the next level.

There are certain legal inhibitions which has been identified as a challenge to develop ICM in the Maldives. Some of these issues are highlighted in Table 3 (below).

Table 3: Legal Inhibitions

Legislation/Regulation	Section/Paragraph	Issue
Land Act (2002)	18 (d) For every land sale effected private person, a tax of 15 percent of the sale price would be levied.	This makes it costly for private people to transfer land for the purpose of issue sukuk.
Land Act (2002)	18 (c) A land bought and registered under the name of a	This means that if a sukuk is made on a land

	<p>hundred percent Maldivian company cannot sell any portion of its shares to a foreigner.</p>	<p>registered under a hundred percent Maldivian owned company, then no portion of that land could be sold to a foreigner. This means that this type of land cannot be an underlying asset of a sukuk that requires selling of land to the sukuk holders as foreigners cannot then be part of this type of sukuk.</p>
Land Act (2002)	<p>It is unsure whether an undivided portion of land could be sold to a group of people.</p>	<p>Common ownership is essential for some sukuk structures if it involves selling of undivided portion of the land to the sukuk holders.</p>
Companies Act (1996)	<p>The Act expressly states that only a public company could issue shares or debentures to the public. It shall be noted that section 23</p>	<p>Under the existing legal infrastructure, a private company would not be able to issue a sukuk unless and until</p>

	of the Act shall be read with the definition of debenture stated in section 102 of the Act which does not include sukuk in the meaning of the debenture.	this provision of the companies Act is amended by ousting sukuk in the definition of debenture.
Regulation on Islamic Securities Screening (2013)	According to the regulation, it is the company who needs to apply for Shari'ah screening with a fee if it is an already listed company.	Instead of the company listed applying for Shari'ah screening, CMDA could do the Shari'ah screening for all listed companies and reveal the result and let the investors deal with purifying of dividends by giving them the guideline to follow in this regard. This might increase the number of Shari'ah compliant equities in the market.
Regulation on Registration of Shari'ah Adviser (2013)	There is a yearly fee which is required to be paid by every	In the initial phase, having to pay a fee to get registered as a Shari'ah Adviser

	registered Shari'ah Adviser.	may demotivate individuals competent to get registered. As such, the fee requirement could be uplifted until the market takes off.
--	------------------------------	--

Source: Author's own and compiled from Aishath Muneeza (2018); Simmons and Simmons (2013) and SiiA (2011) ¹⁸

In terms of lack of laws required for the development of ICM in the Maldives, there is a need to develop laws to regulate the establishment of SPV and to amend existing laws to enable the SPV to issue sukuk.¹⁹ It is observed that under the current law in the Maldives, the creation of local SPVs is not permissible and the concept of beneficial ownership is also not recognized due to the absence of a trusts law²⁰ in the Maldives.²¹ Further, to introduce new innovative ICM products like crowdfunding and Islamic unit trusts, it is imperative for the CMDA to enact the required rules. Without the legal parameters, it would be difficult for the market to welcome such products. For instance, even to create social impact sukuk, a framework

¹⁸ Simmons and Simmons, "Report on Developing a Sukuk Market in the Republic of the Maldives," Capital Market Development Authority, 2013, [https://beta.cmda.gov.mv/en/publications/report-on-developing-a-sukuk-market](https://beta.cmda.gov.mv/en/publications/report-on-developing-a-sukuk-market;); "Developing a Sukuk Market in the Maldives," 2011, <https://www.cmda.gov.mv/assets/Consultancy-Reports/Sukuk-Market-Final-Report-SiiA.pdf>; Aishath Muneeza, "Establishment of Islamic Capital Market in Jurisdictions with Limited Islamic Financial Services: Case Study of Maldives," *International Journal of Law and Management* 60, no.2 (2018): 373–385.

¹⁹ *Ibid.*

²⁰ See: Akmal Hidayah Halim, "The Legality of a Living Trust as an Instrument for Islamic Wealth Management: A Malaysian Perspective," *IIUM Law Journal* 19, no. 1 (2012): 35-50.

²¹ *Ibid.*

will be important.²² Further, the formation of Capital Market Shari'ah Advisory Council is not provided in the Maldives Securities Act (2006) and therefore, it is questionable whether the Shari'ah opinion given by the Council would be binding on the industry.²³

The Special Economic Zone Act (2014) enables the creation of offshore financial services in the Maldives in the Special Economic Zone (SEZ) with approvals from the SEZ Board of Investment and the MMA. As such, this would be an opportunity to create offshore-offered's ICM products. The lack of laws to provide incentives to the ICM players could be another issue in this regard. It is necessary for the country to provide tax incentives for those involved in the capital markets. For instance, there is a need for the introduction of a law on the formation and regulation of SPVs that enable the SPVs to act as a sukuk issuer.²⁴

In general, there are three types of tax incentives that could be introduced: the possibility for the issuer or the originator of the sukuk to get a deduction for the cost of listing a sukuk from its taxable profits; giving 100% or partial income tax relief for a defined period for sukuk holders who engages in investing in listed sukuk; and full or partial relief from business profit tax for a limited time for advisors, arrangers or underwriters etc. in respect of income derived from advising, arranging or underwriting etc. in respect of a listed sukuk issuance.²⁵

²² See: Mahadi Umar Ahmad, Yahaya Yunusa Bambale and Mahamad Ibrahim Adam Zain, "A Social Impact Bond (SIB): A Shariah Appraisal," *IIUM Law Journal* 27, no. 1 (2019): 181–208.

²³ Aishath Muneeza, "Establishment of Islamic Capital Market in Jurisdictions with Limited Islamic Financial Services: Case Study of Maldives," *International Journal of Law and Management* 60, no.2 (2018): 373–385.

²⁴ Simmons and Simmons, "Report on Developing a Sukuk Market in the Republic of the Maldives," Capital Market Development Authority, 2013, <https://beta.cmda.gov.mv/en/publications/report-on-developing-a-sukuk-market>.

²⁵ *Ibid.*

THE NEED FOR LEGAL REFORM

Amendment to Statutes

Several amendments are required in these legislations for the development of ICM in the Maldives. As mentioned above, as per the land law of the country, foreigners are not allowed to own land in the Maldives and it is suggested that this restriction needs to be amended for the promotion of the ICM given that several ICM products include the transfer of ownership such as sukuk.

At present, only a Maldivian citizen may legally buy and own a freehold land in the Maldives.²⁶ According to the Regulation on Owning and Trading Land in Maldives 2008, the buyer may be a Maldivian citizen, company or co-operative society registered in the Maldives where it is fully owned by the Maldivian citizens or all its members are locals.²⁷ Hence, there is a need for the amendment to the law allowing a foreign company to own land in the Maldives in order to promote and develop ICM products in this country.

Furthermore, section 18(e) of the Land Act²⁸ states that if any dwelling or land is being sold then 15% of the purchase price of the dwelling or the land shall be paid to the government as tax²⁹. ICM products like sukuk involve the transfer of legal ownership from the originator to the issuer followed by the issuer to the sukuk investors. At times, two-layers of sale could involve in the sukuk transactions, triggering the 15% tax will be imposed twice and thus the cost or expenses of sukuk. Therefore, there is a need for the amendment of the Land Act in the Maldives to provide exemption to sukuk and other Islamic finance related transactions.

²⁶ See: Section 18(d) Maldives Land Act No. 01/2002.

²⁷ See: Section 9(c) Regulation on Owning and Trading Land in Maldives, Maldives' Constitution of 2008.

²⁸ Maldivian Land Act.
<https://www.mvlaw.gov.mv/pdf/translation/Land.pdf>

²⁹ See: Section 18(e) Maldives Land Act No. 01/2002.

Statutory Recognition of Capital Market Shari'ah Advisory Council

The Regulation on Capital Market Shari'ah Advisory Council (2013) is silent on whether the Shari'ah ruling provided by the Council is binding or not on the board of directors of the CMDA, the industry and the court. Therefore, the Shari'ah rulings provided by the Council may be rejected by the board of directors of CMDA or the industry or even by court. Therefore, legal certainty on the effect of the ruling provided by the Council is important for the sustainable development of ICM in the country.

Higher Standards for Protection of Retail Investors

Another vital legal reform that should be taken into consideration by the Maldives government is to have higher standards of protection for the retail investors. Basically, there are two types of investors namely retail investors and sophisticated investors. A pensioner or a person saving money for children's education is generally called retail investor who chose to invest these monies in sukuk.

A sophisticated investor is a person whose wealth or income are above a certain limit. For instance, in Malaysia, if a person's net asset is worth more than RM3 million, or his annual gross income is more than RM300,000 then he is considered a High Net worth Individuals.³⁰ Generally, sophisticated investors have their own investment manager, financial advisors, and lawyers. On the contrary, retail investors have

³⁰ See: Section 229 (Schedule 6) (Part A) (C) (13) of Capital Market Services Act 2007 (Act 671) (a) whose total net personal assets, or total net joint assets with his or her spouse, exceed three million ringgit or its equivalent in foreign currencies, excluding the value of the individual's primary residence; (b) who has a gross annual income exceeding three hundred thousand ringgit or its equivalent in foreign currencies per annum in the preceding twelve months; or (c) who, jointly with his or her spouse, has a gross annual income exceeding four hundred thousand ringgit or its equivalent in foreign currencies per annum in the preceding twelve months.

no such capacity and because of that, there is a need for a higher protection for their investments.

For example, the HDFC *Mudarabah* sukuk was marketed to both retail and sophisticated investors and both groups received the same treatment which was to the disadvantage of the retail investors. There are several issues in this sukuk issuance. In the HDFC sukuk, less investor protection and minimal information have been provided in the sukuk prospectus. In the HDFC *Mudarabah* sukuk, investor is the *rabbul mal* whereas the HDFC Amna is the *mudarib* or entrepreneur where the investor has to bear all the risks. The HDFC Amna will not be responsible for any losses unless and until there is negligence on the part of the HDFC Amna. The important question here is what amounts to 'negligence' which is silent in the prospectus. The issue of negligence shall only be left to be decided by the court of law. There are fiduciary duties owed by the *mudarib* to the *rabbul mal*. Once the fiduciary duty is breached then only negligence will be triggered. Therefore, duties must be expressly mentioned in the prospectus. For instance, the prospectus must state whether the sukuk proceeds will be collateralized and if the proceeds have been utilized without collateralization it may amount to a breach of fiduciary duty. Furthermore, the leverage level of the sukuk proceeds must be expressly stated in the prospectus and the debt ratio shall not be more than two. With this standard, the prospect retail investors of the sukuk will feel secure enough to invest in the sukuk issuance. The current practice however seems to be loose as no clause has been expressed in the prospectus regarding how the negligence will be established against HDFC which affects the confidence of the retail investors which needs to be rectified by the law.³¹

In addition, investment products are not available to be purchased by the retail investors unless certain criteria are met. High risk or complex products shall not be marketed to retail investors. Products marketed to retail investors must provide detailed graphs and illustrations either in the prospectus or brochures with examples of its *modus operandi*.³²

³¹ Interview with Informant.

³² *Ibid.*

Similarly, the HDFC sukuk has been issued by using an investment contract i.e., *Mudarabah* contract, and the consumer protection or protection of investor funds has been used in the HDFC sukuk which can be an example to another issuer. Nonetheless, after scrutinizing the practice of the HDFC sukuk, it is not easy to decide at what level the investor protection has been made.³³ For instance, from the prospectus, it is unknown how the sukuk proceeds will be utilized. When utilizing the sukuk proceeds, it is unknown in the prospectus as to which level of credit underwriting criteria will be followed. Likewise, the prospectus is also silent on whether there will be any collateral or not. Not only that, the prospectus does not say how the fund will be invested based on the creditworthiness of investors, which is not in the prospectus or any other public document that people can read³⁴. The impact is that when this information is not known to the public it will fall under the English Equity Principle in case of any dispute. Under the equity principle, the court will establish a fiduciary duty, either standard duty of care, or utmost duty of care. These principles are not well-established principles in the Maldivian case law including the tort principles.³⁵ Therefore, in case of default of the sukuk, considering the current Maldivian legal system, it is not easy to get justice by using the aforesaid equitable principles. In addition, no such information has been provided in the prospectus. Therefore, detailed information must be provided in the sukuk prospectus that enables retail investors to make an informed decision.

Sukuk are based on investment contracts and there are two main types of investment contracts, *Wakalah* and *Mudarabah*. In these contracts, there is a great need for investor or consumer protections.

Mostly, in other countries, they have categorized the investors into two main categories: retail investors and high net worth individuals. There is a minimum standard required if the product is targeted to the retail market. In this standard, the fiduciary duty is very high on the product issuer.³⁶ They must ensure utmost duty of care towards retail

³³ *Ibid.*

³⁴ *Ibid.*

³⁵ *Ibid.*

³⁶ *Ibid.*

investors.³⁷ In case of sophisticated investors, the investor has the option to demand the product issuer to provide the necessary information in the prospectus if it is not there.³⁸ In Malaysia, for example, the retail market is protected by investor protection framework comprising:

“A robust disclosure regime which includes prospectus and continuous disclosure requirements and checks and balances in the form of a trustee and trust deed; Mandatory credit rating for all bonds and sukuk that are offered to the retail market by a registered credit rating agency; and Investor education initiatives to enhance investor understanding and knowledge of investing in bonds and sukuk. Certain categories of issuers may be exempted from some of these requirements e.g. Malaysian Government or government guaranteed issuances.”³⁹

If a sukuk has been issued to the retail market, then the prospectus must have much more detailed information, and there is a great need for the improvement of the current prospectus. The information provided in the prospectus must be well enough that enables the retail investor to make a well-informed decision.

Why do we need to have such detailed information in the prospectus? The lower financial literacy among the public means that there will be a higher chance of misappropriation of public funds. Certain level of investment products must be prohibited in issuing to the retail market unless and until financial literacy has been promoted to a certain level, or it can be stated that a product can only be bought by someone who has the accounting knowledge, or it can be stated that the product can only be bought with the assistance of someone who has the knowledge of accounting background which was agreed by the majority of the informants.⁴⁰

³⁷ *Ibid.*

³⁸ *Ibid.*

³⁹ “Frequently Asked Question on Retail Bonds and Sukuk,” Securities Commission Malaysia, accessed September 9, 2018, <https://www.sc.com.my/frequently-asked-questions-on-retail-bonds-and-sukuk>.

⁴⁰ Interview with Informant.

Establish Offshore Centre to Develop ICM in the Maldives

To become a regional hub for Islamic finance, the Maldives needs to open their market to the international arena including India, Seychelle, Mauritius, Hong Kong, Sri Lanka and other neighboring countries for a wider target market of investors. The Maldives may target to become the domicile place for the sukuk issuance in the region since the nation is one of the most attractive places for sukuk domicile. When sukuk is domicile in the Maldives, when there is any dispute, it will be governed by the Maldives Laws and Regulations.

There are several advantages for making the Maldives a domicile place in sukuk issuance and a hub in Islamic finance in the region. Among the reasons include the Maldives' low tax regime, less disclosure requirements, less stamp duty, high privacy, Shari'ah compliant laws and regulations, Shari'ah courts, and not much challenges in issuing Shari'ah compliant products.⁴¹

At present, off-Shore centres could be found in the British Virgin Islands, and Seychelles. Now the question is how to make the Maldives one of these off-shore centres. Existing limitation is that the Maldives does not have the infrastructure to become an off-shore centre. However, there are strategic benefits available to the Maldives as it is a hundred percent Muslim country and implementation of Shariah and enforcing the Shariah compliant contracts in the courts would be easy than that in a secular country. The Maldives Constitution is also based on Shari'ah. All the courts are Shari'ah Courts. Almost all the judges are familiar with Shari'ah principles. These features are hardly found in any other part of the region. The Maldives itself is a very good brand in the international market.

⁴¹ *Ibid.*

Amendment of Fund-Raising Limits

There is another hindrance to a private company to become a public company in the Maldives. If a private company wishes to become a public company, it must have a paid-up capital of MVR 1 million.⁴² Only a public company is allowed to issue shares to the public.⁴³ If a public company wishes to issue such shares, it can raise a maximum amount equivalent to its paid-up capital in Initial Public Offering (IPO).⁴⁴ If the paid-up capital was MVR1 million, then it can raise only another MVR1 million, totaling MVR 2 million as share capital. Now the question is whether it can do a Follow-on Public Offer (FPO). According to section 23 of the Companies Act, FPO also cannot be made.

This requirement of limiting the capacity to raise the IPO or FPO amount up to the paid-up capital is another hindrance to private companies to become public companies. Hence, this is also another hindrance to the development of ICM in the Maldives.

Enactment of Trust Act

Another major challenge to the development of ICM is the absence of legislation on trust in the Maldives. When establishing an SPV, there is no way that the SPV can be established as a single shareholder as the company law requires a minimum of two shareholders. The SPV must be appointed as a trustee. According to the Companies Act there must be a minimum of two shareholders based on the general principles of company law. It is suggested that, for the convenience of record keeping, a separate company can be created. For example, for construction of one condominium, a separate company can be established. The same analogy can be used in sukuk. If the originator wishes to build a hospital, school, and bridge, three separate SPV can be created to issue the sukuk.

⁴² See: Section 7 and 20 the Companies Act No. 22/1996

⁴³ See: section 23 the Companies Act No. 22/1996

⁴⁴ See: section 23 the Companies Act No. 22/1996

Moreover, according to the latest IFRS Accounting Standards, if one of its investments has been disposed of, then the accounting treatment will affect the whole company's accounting treatment.⁴⁵ If different companies or SPVs are created for each project, then it does not affect the whole company's accounting treatment. And these companies or SPV need not have two shareholders; it can be done with two shareholders only.

In the absence of the Trust Act, there is an issue of ownership. There are two types of ownership: beneficial ownership and legal ownership. When a transaction is made appointing a party as a trustee, then a such relationship shall be governed under a Trust Act. Once SPV is created, the legal ownership will be transferred to the SPV. If the legal ownership has been transferred without appointing a trustee, there is a risk that the legal ownership of the underlying property being lost from its originator if the legal transfer has been made without the transferee being appointed as a trustee.

Even if the legal ownership of the underlying property has been transferred to the SPV as a trustee, there will be a fiduciary duty owed by the SPV as a trustee. Once the purpose of the creation of the SPV has been fulfilled, there will be a duty of the SPV to transfer the legal ownership of the underlying property to the originator. Also, as the trustee, it has a duty to maintain the underlying property according to the agreed terms. For example, the Maldives Centre for Islamic Finance (MCIF) has been entrusted with the role of SPV. The underlying asset may be the 25-storey hospital building. The legal ownership will be transferred to MCIF.

⁴⁵ Interview with Informant.

However, the government must ensure that the intended purpose of the building will remain, and the property will be held in trust by the MCIF for the government of Maldives. Therefore, in sukuk, the legal ownership has been transferred to the SPV and the beneficial ownership remains with the originator. In the Maldives, all these legal relations are managed by the terms and conditions of the contract and under contract law. Hence, there is an urgent need for a Trust Act in the Maldives.

CONCLUSION

In conclusion, ICM in the Maldives is small but it has significant potential and is indeed a promising market. The ICM has been undergoing several developments with a number of regulations and guidelines have been issued by the relevant authorities. There is a huge potential for the Maldives to attract foreign investors in the ICM. The present initiatives however are not sufficient for the Maldives to excel in ICM. Urgent actions need to be taken to investigate several laws and consider the necessary amendments to facilitate ICM in the Maldives. These include the regulations relating to tax, investors protection, fundraising limit as well as incentives for companies to go public and participate in ICM.

On the Shari'ah aspects, the regulations must also facilitate the issuance, promotion, and trading of Islamic securities. There must be a clear policy on Shari'ah compliance and Shari'ah governance for ICM. The role of the Shari'ah advisory body needs to be properly recognized as the main reference for matters relating to Shari'ah and Islamic law on ICM. Internal good governance system is to be adopted to ensure Shari'ah compliance aspects of the operation, management, and trading of ICM products and instruments.

Attracting investors is also one of the main aspects that the government of Maldives needs to pay attention to. The country's strength as the world tourist paradise that attracts high dollar turnover in the tourism industry is to be positively exploited for creating active participation of investors in ICM. Thus, a complete ecosystem must be enhanced and a robust ICM regulatory framework needs to be explored. It is anticipated that the findings of this research would assist

policy makers to bring the required changes to ICM in the country to untap the potential of it.