AAOIFI Financial Accounting Standard (FAS) 46

Off-Balance-Sheet Assets Under Management

Contents

AAOIFI Financial Accounting Standard (FAS) 46 "Off-Balance-Sheet Assets Under Management" is set out in paragraphs 01-29. All the paragraphs have equal authority. This standard should be read in the context of its objective and the "AAOIFI Conceptual Framework for Financial Reporting". It shall also be read in conjunction with FAS 44 "Determining Control of Assets and Business" and FAS 45 "Quasi-Equity (Including Investment Accounts).

All AAOIFI FASs shall be read in conjunction with the definitions, Shari'ah principles and rules and key considerations provided by AAOIFI Shari'ah Standards in respect of such products and matters.

Preface

PR1 Under their unique business model, Islamic financial institutions (the institutions) issue investment instruments (including maintaining investment accounts and issuing other instruments / securities) under various profit or loss sharing (or taking) arrangements. Such arrangements are usually based on Islamic finance participatory structures, such as Mudaraba, Musharaka or Al-Wakala Bi Al-Istithmar.

PR2 These participatory investment instruments represent funds received by an institution for investment on behalf of the investors and may or may not include restrictions regarding how such funds are invested. The relationship between the institution and such investors vary according to the terms of the respective contract and, at times, is limited to management of such investments without having control, as per AAOIFI’s financial reporting framework, and hence qualify for off-balance-sheet accounting.

PR3 This standard improves upon, and brings at one place, the requirements related to financial reporting of off-balance-sheet assets under management.

PR4 This standard along with FAS 45 “Quasi-Equity (Including Investment Accounts)” supersedes the earlier FAS 27 “Investment Accounts”.

Introduction

Overview

IN1 This standard prescribes the criteria for characterisation of off-balance-sheet assets under management, and the related principles of financial reporting in line with the "AAOIFI Conceptual Framework for Financial Reporting" (the conceptual framework).

IN2 The standard encompasses the aspects of recognition, derecognition, measurement, selection and adoption of accounting policies, etc., related to off-balance-sheet assets under management, as well as, certain specific aspects of financial reporting, e.g., impairment and onerous commitments by the institution. The standard also includes the presentation and disclosure requirements, particularly aligning the same with the requirements of FAS 1 "General Presentation and Disclosures in the Financial Statements" in respect of the statement of changes in off-balance-sheet assets under management.

IN3 This standard, along with, FAS 45 "Quasi-Equity (Including Investment Accounts)", supersedes the earlier FAS 27 "Investment Accounts".

Rationale for issuing this standard

IN4 In view of the recommendations of the comprehensive AAOIFI Financial Accounting Standards (FASs) review and revision project, as well as, the need for alignment of existing AAOIFI FASs, the AAOIFI Accounting Board (AAB / the board) decided to revise FAS 27 "Investment Accounts". The initial study identified various aspects in which the financial reporting requirements needed to be enhanced and specific aspects to be covered with regard to the off-balance-sheet assets under management. The board particularly considered the need for alignment with certain changes brought in by FAS 1 "General Presentation and Disclosures in the Financial Statements" and recognised the increased significance of the subject with increasing use of Al-Wakala Bi Al-Istithmar by the institutions.

IN5 In view of the same, the board concluded that there is a need for a separate standard for assets managed in a fiduciary capacity without establishing control, which are subject to off-balance-sheet accounting.

Significant changes from previous standard

IN6 This standard brings significant changes from its predecessor standard (FAS 27 "Investment Accounts"), inter alia, in the following aspects:

a. criteria for characterisation as off-balance-sheet assets under management (based on control) is defined and unlike the previous standard, structures other than those based on restricted Mudaraba have been included in the scope;

b. various definitions, such as, in respect of fiduciary capacity, off-balance-sheet assets under management, as well as, off-balance-sheet investment accounts are aligned with FAS 44 "Determining Control of Assets and Business" and "AAOIFI Conceptual Framework for Financial Reporting";

c. the requirements are prescribed for selection and application of accounting policies for the purpose of off-balance-sheet assets under management to be consistent with an institution's overall accounting policies developed in line with the relevant AAOIFI FASs;

d. presentation and disclosure requirements for the institutions are improved including requirement to prepare and present a statement of changes in off-balance-sheet assets under management as a primary financial statement in line with FAS 1 "General Presentation and Disclosures in the Financial Statements"; and

e. certain specific aspects of financial reporting, e.g., impairment and onerous commitment situations have been included.

AAOIFI Financial Accounting Standard (FAS) 46
Off-Balance-Sheet Assets Under Management

Objective of the standard

1. The objective of this standard is to establish the principles of financial reporting related to off-balance-sheet assets under management in line with the "AAOIFI Conceptual Framework for Financial Reporting[1]" (the conceptual framework).

Scope

2. This standard shall be applicable on all Islamic financial institutions (the institutions) preparing financial statements in line with the requirements of AAOIFI Financial Accounting Standards (FASs), with regard to the assets managed in a fiduciary capacity without establishing control, except for:

    a. the participants' Takaful fund and / or participants' investment fund of a Takaful institution[2]; and

    b. an investment fund managed by an institution, being a separate legal entity, which is subject to financial reporting in line with the requirements of the respective AAOIFI FAS[3].

Definitions

3. For the purpose of interpreting and applying this standard, the following short definitions are relevant:

    a. Fiduciary capacity – is the capacity to act, in good faith, on behalf, and for the benefit, of another party with a duty to preserve trust;

    b. Off-balance-sheet assets under management – include assets held, managed, administered or otherwise dealt with in an arrangement that gives an institution a fiduciary responsibility but not control[4];

    c. Off-balance-sheet participatory investment instruments (including investment accounts) – are the participatory investment instruments (including investment accounts) whereby the underlying assets meet the definition of off-balance-sheet assets under management and hence, the institution does not control the same; and

    d. Participatory investment instruments – in the specific context of this standard, include all instruments (particularly including investment accounts) whereby the investors are entitled to share / take the profit and bear the risk of loss and are entitled to a residual interest in the underlying assets or business (commonly referred to as an investment pool), in line with Shari'ah principles and rules.

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[1] "AAOIFI Conceptual Framework for Financial Reporting"
[2] The accounting and financial reporting for participants' Takaful fund and participants' investment fund of a Takaful institution shall be in line with their requirements of relevant AAOIFI FASs on Takaful.
[3] Presently, FAS 14 "Investment Funds". Also see [ED of] FAS __ "Financial Reporting for Islamic Investment Institutions (Including Investment Funds)".
[4] See paragraph 50 of "AAOIFI Conceptual Framework for Financial Reporting".

Criteria for characterisation as off-balance-sheet assets under management

4. Participatory investment instruments may be divided in two main categories. First, whereby the institution controls the underlying assets, which are classified as quasi-equity instruments. Second, whereby the institution does not control the underlying assets, and manages the same only in a fiduciary capacity, which are classified as off-balance-sheet investment instruments.

5. In order to be characterised as off-balance-sheet assets under management, a participatory investment instrument shall be subject to the conditions specified below:

    a. the institution manages participatory investment instrument (and related liabilities, and resulting income and expenses, including gains and losses) on behalf of investors only under a fiduciary capacity. The common structures used for these instruments are based on Al-Wakala Bi Al-Istithmar (investment agency), restricted Mudaraba and other similar arrangements[5];

    b. in case of participatory investment instruments, it is entitled only to a fee (fixed or variable) (which may additionally include incentives out of profit[6]), share of profit or a combination thereof, according to the Shari'ah principles and rules, as remuneration against management of the underlying assets. However, the institution is not entitled to any residual interest in the underlying assets, except to the extent of such established remuneration;

    c. it does not control participatory investment instruments, in line with the definition of control[7], and hence, is not entitled to or exposed to the variable returns from its involvement with such underlying assets;

    d. a Mudaraba shall be considered a restricted Mudaraba, if and only if, the Rab-ul-Maal has reasonably restricted the independent decision-making powers of the Mudarib in respect of management of the Mudaraba investments. The conditions specified in paragraph 5 shall be tested against the following common criteria:

        i. specifying an asset pool separately from the common assets of the institution, without commingling with the institution's own funds or unrestricted Mudaraba investments, etc.;

        ii. defining an investment boundary, e.g., through defining investment motive, market, platform, risk appetite, assets or asset classes, liquidity profiles, currency, geographical distributions, customer or customer classes; and

[5] In certain rare circumstances, an unrestricted investment account may also be considered as off-balance-sheet asset under management. See Table 1: Examples of applying principles that establish control (by the working partner / agent) for various participatory and agency structures of FAS 44 "Determining Control of Assets and Business". Similarly, there can be certain Wakala / agency based structures that may fall in this category.

[6] Fixed agency fee may include a one time or period-linked fee. Variable fee may generally include a fee based on total revenue / receipts or based on the amount of asset under management, as well as, incentive fee. Incentive based fee, which is a type of variable fee, is normally due in addition to a fixed fee (or other form of variable fee) and is based on the performance of the underlying assets (generally subject to a determined minimum performance benchmark).

[7] See paragraph 5 of FAS 44 "Determining Control of Assets and Business".

iii. restricting the powers of the Mudarib with regard to the replacement, transfer, and / or reinvestment of the Mudaraba assets / funds (as referred to in (i) and (ii) above); and

e. the off-balance-sheet assets under management managed by the institution on behalf of investor(s) shall be considered a separate virtual reporting entity[8] for recording, monitoring and reporting purposes.

Recognition, measurement and derecognition

6. In paragraphs 8-20, recognition, subsequent measurement and derecognition refer to the act of recording and measuring and removal of the assets and related transactions from the virtual reporting entity (distinct and separate from the institution's assets under control). It is clarified that off-balance-sheet assets under management are not recognised by the institution as its own (or under control) assets.

Selection and adoption of accounting policies

7. The accounting policies applied by an institution for the purpose of off-balance-sheet assets under management shall be consistent with its overall accounting policies developed in line with the relevant AAOIFI FASs, unless use of such accounting policies results in an accounting mismatch or does not reflect the business model of the off-balance-sheet assets under management. In such case, the accounting policies selected and adopted shall be in line with the relevant AAOIFI FASs.

Initial recognition

Timing of initial recognition

8. An institution shall initially recognise the investors' managed funds (of the off-balance-sheet assets under management) in a separate virtual reporting entity when the following criteria are met:

    a. cash or cash equivalents have been received by the institution under a legally enforceable contract meeting the definition of off-balance-sheet assets under management; or

    b. when the funds (or corresponding assets) received are transferred to the virtual reporting entity, on the effective date of the contract, as per contractual terms; and

    c. the respective contract has no other precondition to come into effect.

Initial recognition of investors' managed funds

9. The initial recognition of the investors' managed funds of off-balance-sheet assets under management shall be at the fair value of the consideration received when the contract comes into effect.

[8] See BC1 and BC2 of FAS 40 "Financial Reporting for Islamic Finance Windows" for discussion on virtual reporting entity.

Initial recognition of underlying assets acquired

10. An institution shall recognise acquisition of an underlying asset(s) according to the accounting policies adopted for the purpose of off-balance-sheet assets under management, in line with the relevant AAOIFI FASs, when it acquires the asset(s).

Subsequent measurement

Subsequent measurement of the investors' managed funds

11. Subsequent measurement of the investors' managed funds of off-balance-sheet assets under management at the end of a reporting period shall reflect the residual interest in net underlying assets.

Subsequent measurement of underlying assets (and liabilities)

12. An institution shall subsequently measure underlying asset(s) (and any related liabilities, if any) according to the accounting policies adopted for the purpose of off-balance-sheet assets under management, in line with the respective AAOIFI FAS.

Impairment and expected credit losses / write-offs attributable to underlying assets

13. Impairment and expected credit losses / write-offs attributable to the underlying assets shall be recognised according to the accounting policies adopted for the purpose of off-balance-sheet assets under management, in line with the respective AAOIFI FAS, respective Shari'ah principles and rules and contractual terms.

Reserves

14. An institution may create a risk reserve(s) in the virtual entity[9] in line with FAS 35 "Risk Reserves" to mitigate various risks faced by the investors of the participatory investment instruments.

15. Where a reserve is maintained for the off-balance-sheet assets under management, the impairment and expected credit losses / write-offs and fair value losses pertaining to the underlying assets may be set off against such reserves.

Provision for loss due to negligence, misconduct and / or breach of contractual terms to be recognised by the institution

16. Loss due to negligence, misconduct and / or breach of contractual terms on the part of the institution, as established in line with the Shari'ah principles and rules, shall be borne by the institution and hence shall not be recorded as a loss for the virtual reporting entity.

Reassessment by the institution

17. In rare circumstances, the institution may need to inject its own funds in the participatory investment instrument, especially in the case of bridge financing or when the put option is exercised (partially) by the investor(s) before the maturity of the underlying asset. In such cases, the institution shall make a reassessment whether the funds are in the nature of:

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[9] A virtual entity comprises a distinct set of assets and liabilities pertaining to unique set of stakeholders, without taking the form of a legal entity.

a. receivable by the institution, and payable by the virtual reporting entity and are not eligible for accrual of any return and proportionate ownership is acceptable and ascertained; or

b. investment in the institution is in the nature of, and at par with, the other equity investors of virtual reporting entity; or

c. multi-level investment arrangement exhibiting the characteristics described in respective AAOIFI FAS[10] are to be presented accordingly.

Institution's exposure to loss under onerous commitments

18. In certain cases, the institution may be exposed to a risk of loss arising from the onerous commitment arising from underlying assets. This situation usually occurs when:

    a. the life of the underlying asset is more than the contractual term of the participatory investment instrument; and

    b. the underlying asset is expected to have a value lower than the current carrying value at the time the underlying asset reverts to the institution, probably resulting in a loss to the institution at that time.

19. The loss referred to in paragraph 18 shall be recognised in a timely manner and charged to the statement of income of the institution.

Derecognition

20. The investors' managed funds of off-balance-sheet assets under management and the underlying assets are derecognised from the virtual reporting entity when these satisfy the following criteria:

    a. the control of the asset is transferred to another party through sale or otherwise (e.g., through gift or settlement); or

    b. there are no future economic benefits expected from use or disposal of such asset (e.g., if the asset is expired or surrendered or the asset is destroyed or fully impaired); or

    c. the underlying contract is terminated, and there are no further legally enforceable obligations in the virtual reporting entity.

Presentation and disclosures

Disclosure of accounting policies

21. The accounting policies applied to the off-balance-sheets assets under management, if different from the accounting policies applied by the institution, shall be identified and disclosed in the notes.

Statement of changes in off-balance-sheet assets under management

Presentation in the primary financial statements of the institution

22. An institution shall prepare and present a statement of changes in off-balance-sheet assets under management as part of its primary statements at each period end. The statement shall include the

[10] See paragraph 36 of FAS 45 "Quasi-Equity (Including Investment Accounts)".

requirements of the respective AAOIFI FAS[11]. The off-balance-sheet participatory instruments shall be presented on a combined basis in the statement.

23. The statement of off-balance-sheet assets under management shall provide adequate disclosures by asset-type (and related liabilities) in a suitable manner.

24. The disclosures of the following are generally relevant for the purpose of the statement of off-balance-sheet assets under management[12]:

   a. balance at the beginning of the period;

   b. investors' additional capital received during the period;

   c. withdrawals / divestments and maturities of investors' managed funds during the period;

   d. net profits / losses during the period, including:

      i. revenues;

      ii. expenses;

      iii. fair value gains / losses;

      iv. impairments and expected credit losses[13] or write-offs (net of reversals), if any; and

      v. institution's agency fee / Mudarib's share.

   e. transfers to / from the risk reserves during the period;

   f. distributions of profit during the period; and

   g. balance at the end of the period.

Disclosures of changes in off-balance-sheet assets under management for significant virtual reporting entities

25. An institution shall disclose appropriately (in form of individual statements or detailed disclosures), as part of the notes to the financial statements, the information required in paragraphs 22-24 for each material virtual reporting entity. [Explanation: Material virtual reporting entity for the purpose of this paragraph shall be any virtual reporting entity having net assets in excess of 10% of total equity of off-balance-sheet assets under management or in excess of 5% of the total equity of the institution.]

26. In case a financial statement for a virtual reporting entity is required then the same shall be presented in line with the requirements of relevant AAOIFI FASs[14] depending on the nature of underlying assets.

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[11] paragraphs 136 -139 of FAS 1 "General Presentation and Disclosures in the Financial Statements"
[12] Another approach towards measurement and presentation is acceptable, insofar as, the same is in line with the relevant accounting policies developed according to the relevant AAOIFI FASs and the requirements of this standard.
[13] Accounting policies shall be developed according to FAS 30 "Impairment, Credit Losses and Onerous Commitments".
[14] Either FAS 14 "Investment Funds" or FAS 34 "Financial Reporting for Sukuk-holders"

Additional disclosures

27. The institution shall disclose the following additional information in the notes to the financial statements:

    a. provision for onerous commitment in case of expected losses in the value of the underlying assets in case of a probable reversion of the underlying asset(s) to the institution;

    b. any recourse available to any of the investors against a potential loss;

    c. the details of ring-fencing arrangement, if any; and

    d. details of any Hiba, gift, or waiver of fee by the institution to the virtual reporting entity.

Effective date

28. This standard shall be effective for the financial periods beginning on or after 1 January 2026. Early adoption is encouraged. This standard shall be adopted at the same time as adoption of FAS 45 "Quasi-Equity (Including Investment Accounts)".

Amendments to other standards

29. This standard, along with, FAS 45 "Quasi-Equity (Including Investment Accounts)" shall supersede FAS 27 "Investment Accounts".

Appendices

Appendix A: Adoption of the standard

This standard was presented for approval in the 36th AAOIFI Accounting Board meeting held on 12-13 Jumada II 1445H, corresponding 25-26 December 2023 and was duly approved.

Members of the board

1. Mr. Hamad Abdulla Al Oqab – chairman
2. Mr. Syed Najmul Hussain – deputy chairman
3. Mr. Abdelhalim Elsayed Elamin
4. Mr. Abdulmalik Alsuwayni
5. Dr. Abdulrahman M. Alrazeen
6. Ms. Amal Al Masri
7. Dr. Bello Lawal Danbatta
8. Mr. Firas Hamdan
9. Mr. Hondamir Nusratkhujaev
10. Mr. Imtiaz Ibrahim
11. Mr. Irshad Mahmood
12. Dr. Muhammad Albeltagi
13. Mr. Saud Al Busaidi
14. Mr. Sezayi Toprak
15. Mr. Yusuf Ahmed Ibrahim Hasan

Reservation

The standard was approved unanimously.

Working group members

1. Ms. Amal Al Masri – chairperson
2. Mr. Ali Chreif
3. Dr. Anwar Misbah Soubra
4. Mr. Dalip Kaul
5. Mr. Imtiaz Ibrahim
6. Dr. Inza Putra
7. Mr. Jamil Ahmed Shaikh
8. Mr. Mahesh Balasubramaniam
9. Mr. Mohammed J. Hassan Ebrahim
10. Mufti Irshad Ahmed Aijaz
11. Mr. Muhammad Islam Ahmed
12. Mr. Pravin Manik
13. Mr. Saud Al Busaidi
14. Dr. Yosita Nur Wirdayanti
15. Mr. Yusuf Ahmed Ibrahim Hasan

Executive team

1. Mr. Omar Mustafa Ansari (AAOIFI)
2. Mr. Mohammad Majd Bakir (AAOIFI)
3. Mr. Haroon Tabraze (Senior Consultant-Researcher)
4. Ms. Farida Cassim (AAOIFI)
5. Ms. Saira Shamsie (Senior Consultant-Researcher)

Appendix B: Illustrative statement of changes in off-balance-sheet assets under management

[Name of IFI]
Statement of Changes in Off-Balance-Sheet Assets Under Management
For The Period 31 December 20xx

		Bank balances	Receivables trade-based modes	Ijarah Muntahia Bittamleek	Participatory investments	Investments in real estate	Investments in Sukuk, shares and other securities	Others	Current account with the institution – net	Liabilities (if any)	Total
		---CU in '000---									
Current period											
Balance as at beginning of the period	A	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	(xxxxx)	(xxxxx)	xxxxx
Additions	B	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx
Recoveries / disposals / maturities	C	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)
Net increase / (decrease)	D=B-C	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx
Net income	E		xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx			xxxxx
Mudarib's share	F								(xxxxx)		(xxxxx)
Fixed agency fee	G								(xxxxx)		(xxxxx)
Variable agency fee	H								(xxxxx)		(xxxxx)
Total institution's management share	I=F+G+H								(xxxxx)		(xxxxx)
Distributions / withdrawals	J	(xxxxx)							(xxxxx)		(xxxxx)
Balance as at end of the period	K=A+D+E-I-J	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**(xxxxx)**	**(xxxxx)**	**xxxxx**
Prior period											
Balance as at beginning of the period	A	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	(xxxxx)	(xxxxx)	xxxxx
Additions	B	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx
Recoveries / disposals / maturities	C	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)	(xxxxx)
Net increase / (decrease)	D=B-C	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx
Net income	E		xxxxx	xxxxx	xxxxx	xxxxx	xxxxx	xxxxx			xxxxx
Mudarib's share	F								(xxxxx)		(xxxxx)
Fixed agency fee	G								(xxxxx)		(xxxxx)
Variable agency fee	H								(xxxxx)		(xxxxx)
Total institution's management share	I=F+G+H								(xxxxx)		(xxxxx)
Distributions / withdrawals	J	(xxxxx)							(xxxxx)		(xxxxx)
Balance as at end of the period	K=A+D+E-I-J	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**xxxxx**	**(xxxxx)**	**(xxxxx)**	**xxxxx**

[Note 1: This format is an example of how the statement may be presented. Alternative modes of presentation that are consistent with the disclosure objective may be considered. Distributions could be item-wise or total. A simplified statement can also be made with total assets, total liabilities, less distributions, agency fee, etc. Similarly, liabilities may include funding costs. In such a situation, the amount may be presented in column E of liabilities. Any direct expenses may be shown in column E of cash with adequate disclosures in the notes.]
[Note 2: This is a consolidated statement of all off-balance-sheet assets under management.]
[Note 3: Net income shall include income from investments, fair value gains / losses and attributable expenses. The institution may expand this presentation if such information is considered material for the users of the financial statements.]
[Note 4: Break-up of material items shall be disclosed.]

Appendix C: Basis for conclusions

Criteria for characterisation as off-balance-sheet assets under management

BC1 The board observed that there is a need to establish and clarify appropriate criteria for different instruments including, but not limited to, restricted investment accounts to be considered and accounted for as off-balance-sheet. Therefore, the board concluded to improve the guidance relating to this matter.

BC2 In this regard, the board considered, and concluded, that the criteria and the provisions prescribed by earlier FAS 27 “Investment Accounts”, needed to be aligned with the "AAOIFI Conceptual Framework for Financial Reporting” and FAS 44 “Determining Control of Assets and Business”. The board deemed it imminent to link the criteria for characterisation of investment accounts (as off- or on-balance-sheet) with the concept of control, i.e., any such participatory instrument shall be considered on-balance-sheet when the institution, as a working partner, exercises control over the same, failing which, the instrument will be considered off-balance-sheet. The board further decided to prescribe guidance in this standard in the shape of additional criteria for such characterisation.

BC3 To enhance clarity, and remove any ambiguities, it was also decided to provide assessment criteria to define as to when a Mudaraba structure is of a restricted nature.

Selection and adoption of accounting policies

BC4 A question emerged regarding the applicability of accounting policies to off-balance-sheet assets under management. The board deliberated on whether off-balance-sheet assets under management might have accounting policies that differ from those adopted by the institution. The importance of ensuring consistency and comparability was noted. However, it was agreed that there may be instances where application of a different set of accounting policies to off-balance-sheet assets under management results in faithful representation of the business model under which these off-balance-sheet assets are managed. Consensus was reached that such different policies shall be allowed, if developed according to relevant AAOIFI FASs.

Impairment and expected credit losses

BC5 The working group observed that FAS 30 “Impairment, Credit Losses and Onerous Commitments” excludes off-balance-sheet investment accounts from its scope if, and only if, the institution is not exposed to the risk of losses from such accounts.

BC6 Paragraphs BC22-BC24 of FAS 30 “Impairment, Credit Losses and Onerous Commitments” provide the basis as to why the board concluded to exclude assets within a restricted portfolio managed by an institution from the scope of the said standard, if an institution is not exposed to such risks. This decision stems from the acknowledgment that risks associated with assets within a restricted portfolio are directly attributed to investors, and these assets do not form part of the institution’s owned assets. This exclusion applies only if the institution is not exposed to any form of risk of loss related to assets within a restricted portfolio.

BC7 The board reconsidered the applicability of impairment and expected credit losses (as well as, write-offs) attributable to the underlying assets along with the flexibility provided (as referred to in paragraph BC8), and decided that the impairment and credit losses shall be recognised according to the accounting policies adopted for the purpose of off-balance-sheet assets under management, in line with the respective AAOIFI FAS, respective Shari'ah principles and rules and contractual terms. Accordingly, where suitable such accounting policy shall be in line with the requirements of FAS 30 "Impairment, Credit Losses and Onerous Commitments". However, in the event such off-balance-sheet assets are not subject to such impairment and credit loss accounting, these may be subject to the requirements related to onerous commitments. (See paragraphs 18-19 and BC8-BC10)

Institution's exposure to loss under onerous commitments

BC8 A question arose as to whether an institution may be subject to onerous commitments with regard to probable risks arising from off-balance-sheet assets under management, if the same are not subject to accounting for impairment and credit losses.

BC9 The working group and the board discussed an example wherein a restricted investment account has a duration of five years, while the underlying asset has a tenure of ten years, implying that the asset may probably revert to the institution after five years, and hence the institution may be subject to an impairment or expected credit loss in such situation. This would particularly be the case when the underlying asset is expected to have a value lower than the current carrying value at the time the underlying asset reverts to the institution, probably resulting in a loss to the institution at that time. The working group suggested, and the board agreed, that a provision for onerous commitment on account of any probable impairment or credit losses arising at that time may be necessary to be currently recorded by the institution. Establishing such a provision aligns with a prior technical release (TR) issued by AAOIFI. (See TR 01/2020 "Implementation guidance for AAOIFI FAS 31 "Investment Agency (Al-Wakala Bi Al-Istithmar)"").

BC10 Consensus was reached to incorporate the requirements for recording provision for onerous commitment in such situation in this standard. Consequently, the TR 01/2020 "Implementation guidance for AAOIFI FAS 31 "Investment Agency (Al-Wakala Bi Al-Istithmar)"" stands withdrawn.

Appendix D: Brief history of the preparation of the standard

H1 The AAB held its 26th meeting on 28-29 Rabi' I 1443H corresponding to, 3-4 December 2021. In this meeting the board agreed on the initial output of revision FAS 27 "Investment Accounts". The initial output was agreed to be one standard on quasi-equity and one on off-balance-sheet assets under management.

H2 The working group in its 7th meeting held on 4 Safar 1444H, corresponding to, 31 August 2022 discussed the first version of the draft standard on off-balance-sheet assets under management.

H3 The working group in its 8th meeting held on 15 Safar 1444H, corresponding to, 11 September 2022 discussed the updated draft based on initial comments and observations. After making necessary changes the draft standard on off-balance-sheet assets under management was recommended to the board.

H4 The AAB held its 29th meeting on 29 Safar 1444H, corresponding to, 25-26 September 2022. In this meeting the board requested specific changes and approved, in principle, the exposure draft for issuance.

H5 After incorporation of the specified changes, the exposure draft was issued on 6 Jumada II 1444H, corresponding to, 30 December 2022.

H6 A total of three public hearings (two in English language and one in Arabic language) for the exposure draft were held over the period between March 2023 and December 2023.

H7 The AAOIFI Public Interest Monitoring Consultative Committee (PIMCC) held its 5th meeting on 17 Dhul-Qa'dah 1444H, corresponding to 6 June 2023. No major comments were raised on the exposure draft from the public interest perspective.

H8 The committee of the Shari'ah board for review of accounting and governance standards held its 37th meeting on 8 Muharram 1445H, corresponding to, 26 July 2023 where the exposure draft was discussed duly taking the views for conformity with AAOIFI Shari'ah standards.

H9 A Roundtable for the standard was held on 1 Jumada I 1445H, corresponding to. 15 November 2023.

H10 The working group in its 11th meeting held on 7 Jumada II 1445H, corresponding to, 20 December 2023 discussed all comments received from public hearings along with the views and comments from different industry participants on the exposure draft. After making necessary changes, the standard was recommended to the board for final approval.

H11 The AAB held its 36th meeting on 12-13 Jumada II 1445H, corresponding to, 25-26 December 2023. The board deliberated on changes suggested by the working group and the standard was approved for final issuance.

H12 After completion of the due process, the standard was issued on 18 Jumada II 1445H, corresponding to, 31 December 2023.