[Exposure Draft (GS 2/2021) v13.0 of the]

AAOIFI Governance Standard (GS) ___

Syndicated Financing

Contents

AAOIFI Governance Standard (GS) __ "Syndicated Financing" is set out in paragraphs 1-53.

Where the context so requires, the use of the masculine gender shall include the feminine gender and the singular shall include the plural and vice versa and the word "person" shall include any institution, corporation, firm, partnership, body corporate or other forms of association. The table of contents and headings do not form part of the text of the standard and are for the purpose of convenience and ease of understanding, and may, at times, help in the interpretation of text only. This standard shall be read in conjunction with AAOIFI's Shari'ah Standard (SS) 24 "Syndicated Financing".

Preface

PR1 As a common business practice, Islamic financial institutions (IFIs) form syndicates to meet large-size financing needs of sovereign or corporate customers where a single IFI is not able to finance the whole transaction amount or take such large exposure on a single customer, or other plausible reasons. Moreover, due to various justifiable reasons, including liquidity constraints and balance sheet limitations, IFIs and conventional financial institutions (CFIs) participate in a hybrid syndicated financing transaction comprising of distinguishable tranches of conventional and Shari'ah compliant financing.

PR2 The syndicated financing transactions, whether between IFIs or with CFIs potentially face certain Shari'ah compliance, as well as, governance related issues. While primarily these Shari'ah compliance issues and certain governance issues have been addressed in AAOIFI SS 24 "Syndicated Financing", there are still several governance, control and risk issues which need to be addressed. This standard aims to address such issues to ensure the maximum safeguard of the interests of the parties to a syndicated financing transaction, as well as, its compliance with Shari'ah principles and rules at each transaction stage.

Introduction

Overview

IN1 This standard provides a principle-based framework for the governance of syndicated financing transactions. Such framework is expected to ensure better safeguarding of the interest of the parties to a syndicated financing transaction (through transparency, avoidance of conflict of interest and fair and equitable treatment of stakeholders) and ensuring compliance with the Shari'ah principles and rules over the entire lifecycle of such transactions.

IN2 The standard sets out the essential requirements related to Shari'ah compliance, transparency, fair dealings / avoidance of conflict of interest and other good governance practices as applicable at various stages / phases of a syndicated financing transaction. Such phases include award of mandate, marketing and negotiation, transaction close, continuity of the transaction and its maturity / liquidation (whether early or as per original maturity).

Rationale for this standard

IN3 Due to the involvement of multiple parties and stakeholders and a larger (than normal) amount of financing, syndicated financing transactions are more prone to additional risks from the perspective of Shari'ah compliance, Shari'ah governance, transparency and fair and equitable treatment of stakeholders. Some of these risks are further increased in the case of a hybrid syndicated financing transaction due to the involvement and active role of the CFIs.

IN4 AAOIFI Shari'ah Board issued in 2005 AAOIFI SS 24 "Syndicated Financing" which entails and addresses the Shari'ah principles and rules applicable to such transaction, along with certain governance aspects. However, AAOIFI Governance and Ethics Board (AGEB / the board) identified a need to enhance the requirements of the said standard by addressing certain additional governance, control and risk issues in the form of a comprehensive governance standard. The board particularly noted the absence of a globally accepted mechanism or control framework for IFIs to address such issues, warranting the development of such standard a priority.

IN5 It is expected that the implementation of the governance framework provided by this standard shall enhance the stakeholders' confidence in IFIs and Islamic financial markets. It shall improve the level of compliance with Shari'ah principles and rules and good governance practices, including transparency and fair and equitable treatment of stakeholders.

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Syndicated financing

Objectives of the standard

1. The objective of this standard is to set out a framework for the governance of syndicated financing transactions over the entire lifecycle of such transactions in line with the best governance practices and Shari'ah governance.

2. Implementation of such framework, in turn, is expected to result in enhanced stakeholders' confidence in IFIs and Islamic financial markets, particularly with regard to the compliance with Shari'ah principles and rules, ensuring transparency and fair and equitable treatment of stakeholders.

3. This standard complements and shall be read in conjunction with AAOIFI SS 24 "Syndicated Financing".

Scope

4. This standard sets out the governance framework for the overall lifecycle of syndicated financing transactions comprising deal origination, award of mandate, marketing and placement, financial close till deal termination, whether early or as per the original maturity phases.

5. The responsibility to implement this standard rests with those charged with governance and the management of the lead arranger, syndicate participants and the IFI's customers, in their respective capacities.

6. The guidance provided in this standard, particularly in respect of the pre-mandate phase (also known as the "deal origination" phase) and financial close phase, shall also be applicable, mutatis mutandis, on listed and unlisted Sukuk issuances insofar as the same is not in conflict with GS 12 "Sukuk Governance".

Definitions

7. For the purpose of clarity and interpretation of this standard, and in the specific context of this standard, the following short definitions are relevant:

   a. arranger(s) (also referred to as manager(s) in certain jurisdictions) – is one or more IFI / CFI, individually or collectively, mandated by the customer of a syndicated financing transaction to arrange finance by way of forming a syndicate of eligible IFIs and / or CFIs. An arranger, unless specifically mentioned otherwise, includes a lead arranger (see paragraph 7(h));

b. customer – in the specific context of this standard, is the person availing a financing facility under a Shari'ah compliance mode of financing by way of a syndicated financing transaction;

c. Fatwa – refers to a Shari'ah opinion presented to a person who seeks it with regard to an incidence that has already occurred (the Fatwa incidence) or is expected to occur. It does not refer to answering queries pertaining to hypothetical incidences;

d. hybrid syndicated financing transaction – in the specific context of this standard, is a syndicated financing transaction which includes a Shari'ah compliant tranche, as well as, a conventional financing tranche;

e. information memorandum (also referred to as placement memorandum) – is a disclosure document that describes and presents, for the potential syndication participants, a financing proposal along with the prospective customer's organisational, operational and financial information to facilitate evaluation of such proposal for the purpose of participation as a syndication participant;

f. inter-financier agreement[1] (also, at times, referred to as syndication agreement and / or syndication terms of reference) – is an agreement among the financiers / syndication participants (including IFIs and / or CFIs), or classes of syndication participants, describing, inter-alia, their respective rights and obligations with respect to a syndicated financing transaction, the customer and the underlying assets and / or business (and the respective securities), the details as to how the transaction shall be executed how the payments from the customers are to be received and be apportioned among the syndication participants, etc.;

g. Islamic financial institution (IFI) – is a financial institution that operates in line with Shari'ah principles and rules when performing banking, insurance / Takaful, capital markets and similar activities and includes standalone branches, divisions and windows of conventional financial institutions that offer products and services in line with Shari'ah principles and rules;

h. lead arranger (also referred to as lead mandated arranger or lead manager) – is an IFI / CFI mandated by a customer of a syndicated financing transaction, from amongst the mandated arrangers, to lead the process of arranging a syndicated financing transaction. At times, the responsibility of a lead arranger may be shared by more than one co-lead arranger as per the defined terms of reference in the mandate;

i. mandate (by whatever name called) – is usually the first document to be agreed on a syndicated financing transaction which initiates the syndication process, sets out the

[1] This in essence will serve the same purpose that an Inter-Creditor Agreement serves in a conventional syndicated financing transaction or any other financing deal.

proposed terms of the syndicated financing, and authorises the arranger(s) to arrange the syndicated financing transaction;

j. provisional Fatwa – in the specific context of this standard, is an initial Fatwa issued by the lead arranger's Shari'ah supervisory board (SSB) to approve the basic structure of the syndicated financing transaction that would help the documentation team draft the relevant syndicated financing transaction documents and facilitate the other IFIs' SSBs to have an understanding of the transaction structure;

k. Shari'ah principles and rules – comprise the Shari'ah principles and rules defined by the following hierarchy, as appropriate:

   i. the Shari'ah standards issued by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI);

   ii. the regulations issued by the respective jurisdiction's regulator insofar as these entail the regulatory Shari'ah requirements;

   iii. the rulings of the Central Shari'ah Board for the respective jurisdiction (if one exists);

   iv. the requirements of the applicable Financial Accounting Standards as issued by AAOIFI insofar as these entail Shari'ah related requirements; and

   v. the approvals and rulings given by the Shari'ah supervisory board of the IFI.

l. Shari'ah compliance – is the adherence with Shari'ah principles and rules of the syndicated financing transaction's structure, relevant features, contracts and various other arrangements, as well as, the operations and activities related to the syndicated financing underlying assets during the entire lifecycle of a syndicated financing transaction;

m. syndicated financing (also referred to as consortium financing in certain jurisdictions) – refers to a group of IFIs jointly financing through any Shari'ah compliant mode of financing;

n. syndicated financing underlying assets – are the tangible assets, usufructs and services and / or the ownership of the assets of particular projects or special investment activities, underlying a syndicated financing transaction;

o. security agent (also, at times, referred to as the fiduciary or trustee) – is an entity appointed by the syndication participants (or by the lead arranger on their behalf) to serve as an agent to hold and / or enforce rights on the syndicated financing underlying assets and / or securities on behalf of the syndication participants and to safeguard their interests in accordance with the specific terms of reference;

p. syndication participants (also, at times, referred to as syndicate financiers) – include the IFIs and / or the CFIs agreeing to participate in a syndicated financing transaction; and

q. those charged with governance – in line with the International Ethics Standards Board for Accountants (IESBA) pronouncement, are “the person(s) or organisation(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager”[2].

[2] IESBA pronouncement on the definition of those charged with governance.

Part A: Key pillars and principles for syndicated financing transaction governance

Key pillars of governance applicable to the syndicated financing transaction

8. The key pillars of institutional governance, in line with good practices of governance, as applicable to each syndicated financing transaction, include the following:

   a. Shari’ah compliance – whereby all the organs of governance, including the management, shall ensure that the overall operations of the syndicated financing transaction are in line with Shari’ah principles and rules;

   b. accountability – whereby all the organs of governance, including management, shall have accountability for their respective functions;

   c. fairness – whereby all the stakeholders shall be treated fairly;

   d. transparency – whereby the affairs in respect of the syndicated financing transactions shall be transparent and financial and operational reporting shall be done in a manner that nothing of significance is concealed from respective stakeholders; and

   e. responsibility – the respective parties to the transaction and their organs of governance and management shall function in a responsible manner towards stakeholders and the society / community at large.

Principles of governance

9. The key principles of governance for syndicated financing transactions are summarised in the following table.

No.	Principle	Explanation	Related pillar(s)
1	Effective Shari’ah compliance structures	The syndication participants shall efficiently utilise the existing governance structures to allow for a robust and transparent Shari’ah compliance process during the entire lifecycle of a syndicated financing transaction.	Responsibility Shari’ah compliance
		A syndicated financing transaction, at a minimum, shall comply with the requirements of AAOIFI SS 24 “Syndicated Financing” and other applicable Shari’ah standards.	
2	Fair treatment of, and amongst, stakeholders	The lead arranger, other arrangers and the customer shall ensure fair treatment of, and amongst, different stakeholders.	Accountability , fairness and responsibility

No.	Principle	Explanation	Related pillar(s)
		Those charged with governance and senior management of the lead arranger and the customer shall be accountable to other stakeholders. They shall aim to align, as much as possible, the interests of the stakeholders with the society's interests at large.	
3	Equitable and fair treatment of, and amongst, syndication participants	The lead arranger and the customer shall ensure equitable and unbiased treatment amongst syndication participants, particularly with regard to the distribution of profit and return of capital. As far as possible, the fee sharing amongst the arrangers shall commensurate with the responsibilities and work performed by respective arrangers.	Fairness
4	Transparent interaction of, and amongst syndication participants	Interactions between and amongst the lead arranger, arrangers, syndication participants and the customer shall be transparent at all times.	Transparency
5	Effective oversight	The primary role of those charged with governance of the lead arranger, in a syndicated financing transaction, is to carry out their responsibilities in the best interests of the syndication participants and other stakeholders.	Accountability and responsibility
6	Transparency and mutual disclosures	Syndication participants in general and the arranger(s) in particular shall ensure sharing of timely information pertaining to the customer with each other at all stages of the transaction. The information sharing shall be built upon high transparency and professional ethics standards to build trust with the stakeholders.	Transparency
		The customer shall, at all times during the continuity of the syndicated financing transaction ensure the utmost level of transparency and disclosure in line with the requirements of this standard and the market best practices.	
7	Code of conduct and ethics	All syndication participants in general and the lead arranger and other arrangers in particular shall ensure high ethical standards and adhere to a value-based code of conduct in line with AAOIFI Code of Ethics for the Islamic Finance Professionals and the IFSB Guiding Principles on Conduct of Business for Institutions offering Islamic Financial Services (IFSB-9).	Fairness and responsibility

No.	Principle	Explanation	Related pillar(s)
		The security agent shall act ethically and, in a manner, whereby it does not unreasonably jeopardise the rights and entitlements of the customer.	

Part B: Syndicated financing transaction: parties and lifecycle

Parties to a syndicated financing transaction

10. A syndicated financing transaction generally has the following parties:

    a. the lead arranger;

    b. the arrangers;

    c. the security agent;

    d. the syndication participants; and

    e. the customer.

11. All the parties of a syndicated financing transaction shall be responsible at each respective phase of a syndicated financing transaction for compliance with the requirements of this standard in their respective areas of responsibility.

Lifecycle of a syndicated financing transaction

12. A syndicated financing transaction lifecycle generally comprises of the following phases:

    a. awarding of mandate;

    b. marketing and negotiation;

    c. transaction close;

    d. continuity of the transaction;

    e. changes in the transaction before intended maturity; and

    f. maturity of the transaction.

13. This standard provides the responsibilities of the respective parties to a syndicated financing transaction as applicable at each phase of the syndicated financing transaction lifecycle.

Part C: Considerations at the time of awarding of mandate

Transparency and disclosure

14. At the phase of awarding of mandate (and respective negotiations), a potential lead arranger (and other arrangers) and the potential customer shall exchange all current, relevant and accurate information and / or details about:

    a. the customer, its financial position and operating conditions;

    b. the underlying assets; and

    c. the proposed syndicated financing transaction and its structure.

15. The potential customer shall through an expression of interest request (preferably to be available publicly) disclose in a transparent manner its proposed terms of a syndicated financing transaction and relevant preferences to all the competing potential arrangers so as to provide them a fair opportunity to offer their services.

16. The mandate of a syndicated financing transaction, at a minimum, shall:

    a. document the initiation of the syndication process;

    b. set out the proposed terms of the syndicated financing transaction along with the necessary details about the need for syndicated financing and the underlying assets / transaction;

    c. document the customer's commitment to ensure compliance with the Shari'ah principles and rules, relevant regulations and the requirements of this standard as applicable to the customer; and

    d. authorise the arranger(s) to arrange the syndicated financing transaction;

17. The lead arranger shall procure from its SSB a provisional Fatwa to approve the basic structure of the syndicated financing transaction for the purposes of documentation. The provisional Fatwa shall facilitate:

    a. the proposed syndication participants in gaining confidence in respect of the Shari'ah compliance of the proposed transaction structure, prior to the review of their respective SSBs;

    b. the documentation team in drafting the relevant syndicated financing transaction documents; and

    c. the respective SSBs of the proposed syndication participants to have an understanding of the transaction structure once the final documents are presented for approval.

Conflict of interest

18. A conflict of interest situation may arise at the time of awarding of mandate (and during negotiation for the same), due to:

    a. an existing or a prior customer relationship of a potential arranger with the potential customer (or its associated entities / persons);

    b. an existing financial or non-financial exposure of a potential arranger with the potential customer (or its associated entities / persons);

    c. a fee arrangement between a potential arranger and the potential customer on terms and conditions different from the market norms.

19. A conflict of interest situation may result in jeopardising the interests of either the potential customer or one or more of the potential syndication participants. In order to avoid such a situation:

    a. the negotiation process for awarding of mandate shall be transparent;

    b. the potential arranger(s) shall disclose any possible conflict of interest situation to the potential customer, as well as, to other potential arranger(s) where a mandate is expected to include multiple arrangers; and

    c. the potential arranger(s) shall not accept a mandate to be an arranger if it is probable that such mandate, if so awarded will result in jeopardising the interest of a party or parties of the syndicated financing transaction.

Maintaining Shari'ah compliance in a hybrid syndicated financing transaction

20. Shari'ah compliant syndicated financing transactions should preferably be participated only by the IFIs. However, a hybrid syndicated financing transaction may take place:

    a. if the customer's financing needs cannot be met by IFIs alone (or by IFIs willing to become syndication participants) and hence, require the inclusion of CFI(s); or

    b. if the customer has no specific preference for Shari'ah compliant transactions and has already awarded the mandate to a CFI(s) as arranger(s), and the customer and the arranger(s) are willing to include IFIs as syndication participants by having a separate tranche of Shari'ah compliant financing (to be approved by respective SSBs).

21. In the case of a hybrid syndicated financing transaction:

    a. the sanctity of the Shari'ah compliant tranche shall be maintained under all circumstances, and at all times;

b. the arranger(s) for the Shari'ah compliant tranche shall be clearly identified and shall be only an IFI; and

c. a mandate to such arranger(s) shall be awarded specifically for the arrangement and execution of the Shari'ah compliant tranche in line with Shari'ah principles and rules and the requirements of this standard.

Part D: Considerations during marketing and negotiation

Transparency and disclosure

Information memorandum

22. An information memorandum in line with the market best practices (and regulatory requirements, where applicable) shall be prepared by the arranger(s) and shared with all potential syndication participants on a timely basis.

23. The information memorandum shall, at a minimum, include the following:

    a. a brief about the customer (and where applicable, the syndicated financing underlying assets) including its financial status, past projects, nature of business, market overview and sector performance and outlook;

    b. names and brief introduction of those charged with governance, senior management, as well as, the auditors of the financial statements of the customer;

    c. a detailed feasibility study and market analysis in respect of the customer and the syndicated financing underlying assets;

    d. a detailed description of the syndicated financing transaction, its pricing, necessary financial information and valuation of syndicated financing underlying assets;

    e. where applicable, the phases of the syndicated financing transaction and the total period of completion along with key milestones;

    f. details of profit distribution and loss-sharing mechanism / ratios as applicable to the syndicated financing transaction;

    g. details of the arrangement fee and other relevant service fee(s) payable to the arranger(s) and other parties;

    h. details of the security agent along with its respective rights and obligations;

    i. the potential risks and strategies / instruments to hedge them as applicable to the customer, the syndicated financing transaction and the syndicated financing underlying assets;

    j. a credit and other relevant risks' assessment by the lead arranger with regard to the customer and the syndicated financing underlying assets;

    k. names and brief profiles of the parties providing services related to the syndicated financing transaction e.g., arrangers and guarantee / assurance / Takaful providers;

    l. details of the mechanisms for final settlement and early settlement (before intended maturity);

m. details of recourse to Shari’ah compliant credit enhancement arrangements, including guarantees and undertakings, if applicable, in case of potential default;

n. details of any Shari’ah compliant options attached to the syndicated financing transaction for conversion (to the equity of the customer) or repayment or both, or restrictions on any repayment, as applicable;

o. the applicable legal framework and legal jurisdiction, as well as, dispute resolution mechanism chosen by the parties (including arbitration in line with Shari’ah principles and rules); and

p. a summary of various scenarios that may be applicable to the syndicated financing transaction with regard to early settlement, restructuring or rescheduling, as well as, default (if applicable).

Inter-financier agreement

24. The lead arranger shall prepare in consultation with all potential syndication participants an inter-financier agreement in line with the requirements of this standard[3].

25. An inter-financier agreement, at a minimum, shall include the following:

a. details of the syndicated financing transaction, the customer and the syndicated financing underlying assets, etc.;

b. details of the respective rights and responsibilities of other parties, including, in particular, the syndication participants;

c. details of the lead arranger and other arranger(s) and their respective rights, responsibilities and limitations;

d. details of the security agent and its respective rights and responsibilities;

e. significant details and processes with regard to the security, holding the security / title to the syndicated financing underlying assets and enforcement of rights on the same;

f. summary of the structure and the significant terms and conditions of the syndicated financing transaction (along with the summary term sheet);

g. conditions and process for pre-exit (if so allowed) of a syndication participant (particularly an arranger) and mutual responsibilities in this regard (see paragraphs 45 - 46;

[3] This standard does not seek to prescribe the format of an inter-financier agreement. IFIs are encouraged to follow formats and agreements prescribed by the relevant regulator, if any, or by the standard setting bodies or the market best practices while complying with the requirements of this standard.

h. terms and conditions to ensure equitable treatment of the syndication participants and mutual responsibilities in this regard;

i. rights and responsibilities of various parties in case of early settlement, as well as, upon maturity of the syndicated financing transaction;

j. protocols of sharing information and communication among the syndication participants, in line with the requirements of this standard;

k. conditions and process for transfer of shares of the syndicated financing transaction between the syndication participants; and

l. dispute resolution mechanism applicable amongst the syndication participants.

Inter-financier agreement in case of a hybrid syndicated financing transaction

26. In the case of a hybrid syndicated financing transaction, the inter-financier agreement shall clearly identify and segregate the Shari'ah compliant tranche of the syndicated financing transaction along with a lead arranger(s) with regard to such component of the syndicated financing transaction. Such lead arranger(s) shall, in turn, be responsible to ensure compliance with the requirements of this standard.

27. In such a case, the inter-financier agreement shall ensure proper enforceability of Shari'ah principles and rules, and the independent and equitable status of rights and position of Shari'ah compliant syndication participants. It shall also specify the mechanism in line with the Shari'ah principles and rules applicable in case of default, for the realisation and liquidation of the respective security / syndicated financing underlying assets.

Conflict of interest

28. Pricing for a syndicated financing transaction prior to and during the marketing and negotiation phase may entail a conflict of interest situation due to conflicting objectives and priorities of the arranger(s), the customer and the potential syndication participants.

29. The customer's pricing preferences shall be documented and communicated to the arranger(s). The arranger(s) shall provide, where required, guidance and necessary market information to the customer in this regard.

30. The customer may have preferences with regard to the potential syndication participants. The arranger(s) shall pre-agree and document the customer's preferences before commencing the marketing and negotiation phase. In case the arranger(s), based on its expertise and market understanding, deems it necessary to deviate from the customer's preferences, it should communicate such deviation to the customer along with the rationale for the same.

Part E: Considerations during transaction close

Transparency and disclosure

31. The lead arranger shall consult and keep the customer informed about all major developments in respect of the mandated syndicated financing transaction until the transaction closes. The lead arranger, in particular, shall disclose the following to the customer:

    a. allocation of financing amongst the syndication participants, identifying any preferential allocations or allocations with a potential conflict of interest (e.g., to its associated entities);

    b. the basis of the allocation to the syndication participants, particularly where the total possible participation surpasses the mandated amount of arrangement; and

    c. the details and basis of the underwriting of the syndicated financing transaction by itself or by any other IFI.

32. The lead arranger shall fully apprise the customer of the agreed terms of the syndicated financing transaction, related legal and contractual obligations, as well as, the relevant requirements of Shari'ah principles and rules. The customer shall be allowed reasonable time and opportunity to evaluate the legal contracts to be executed and their potential impact.

33. The arranger(s) and other syndication participants shall preferably, disclose any prior or existing business relationship and relevant experience with the customer. Similarly, a syndication participant, including an arranger with access to customer-related information that may have an adverse impact on the financing decision of other syndication participants, shall share such information with other syndication participants, in accordance with the relevant laws and regulations.

Conflict of interest

34. The arranger(s), at all times, shall ensure that obtaining any additional financing or service business, either directly or by a different department / arm or an associated entity / person, is not leveraged on the mandated syndicated financing transaction in a manner that jeopardises the interests of other syndication participants.

35. The arranger(s) shall ensure that any associated appointments related to the syndicated financing transaction e.g., the security agent or the Takaful service provider, are made on an arm's length basis. The lead arranger may also be appointed as the security agent with the due consent of relevant stakeholders if such appointment does not constitute a conflict of interest.

36. An arranger(s) may be more influenced to close a syndicated financing transaction due to fee income potential for acting in such capacity as compared to other syndication participants. Accordingly, the arranger(s), at all times, shall maintain a high level of professional and ethical conduct and desired level of transparency. It shall also facilitate equitable treatment to all syndication participants.

37. A potential syndication participant who, after being approached by the arranger(s) through any generally established means of communication, decide not to take part in the syndication, shall not:

   a. approach the customer directly to offer a counter-proposal or stand-alone deal; and

   b. divulge, in any manner whatsoever, any material non-public information received about the customer or the syndicated financing transaction.

Part F: Considerations during the continuity of the transaction

Transparency and disclosure

38. The customer shall provide regular progress and performance updates, as well as, periodic financial statements as per the agreed time frame to every syndication participant directly or through the lead arranger or the security agent, as mutually agreed, on a timely basis.

39. All syndication participants, in accordance with the pre-agreed information sharing protocol, shall keep each other updated on any material information that comes to their knowledge with regard to the customer or the syndicated financing underlying assets. This shall include any significant changes in the respective syndication participant's exposure with the customer.

Ensuring Shari'ah compliance during the continuity of the syndicated financing transaction

Respective responsibilities for Shari'ah compliance and governance

40. Each syndication participant shall ensure compliance with Shari'ah principles and rules and shall conform to the requirements of applicable AAOIFI GSs, insofar as, their respective proportionate share in the syndicated financing transaction is concerned. This will inter-alia include the functions and responsibilities of their SSB and their Shari'ah compliance function, internal Shari'ah audit and external Shari'ah audit.

Mutual sharing of issues, observations and knowledge

41. In the case where one of the syndication participants identify an issue or observation with regard to the compliance with Shari'ah principles and rules of a syndicated financing transaction, the respective syndication participant shall immediately inform the lead arranger. The lead arranger, after due consultation with the customer, shall inform all syndication participants about such issue or observation. The syndication participants shall collaborate to reach a solution to such issue or observation.

Change of Fatwa

42. In the case where the SSB of a syndication participant decides to change its Fatwa with regard to the syndicated financing transaction, it shall follow the requirements of AAOIFI SS 29 "Stipulations and Ethics of Fatwa in the Institutional Framework", applicable to a change in earlier issued Fatwa, as well as, [ED of] AAOIFI GS ___ "Shari'ah Decision Making". The respective syndication participant shall promptly inform the other syndication participants and the customer regarding such change in Fatwa. The syndication participants shall collaborate to find a Shari'ah compliant solution to cater to the situation arising from such change in Fatwa.

Part G: Considerations on changes in syndicated financing transaction before intended maturity

Early settlement of syndicated financing transaction

43. Early settlement of a syndicated financing transaction may take place after regulatory clearance and approval of the respective SSBs when:

    a. the parties to the syndicated financing transaction mutually agree to an early settlement of the syndicated financing transaction; or

    b. the customer exercises its unilateral option of an early settlement of syndicated financing transaction in line with the contractual provisions; or

    c. the syndication participants collectively exercise their option of unilateral termination of one or more of the underlying contracts, in line with the contractual provisions, including the option due to default or potential default of the customer on the principal terms of the syndicated financing transaction; or

    d. the regulator orders an early settlement, for any reason that it deems fit.

44. Early settlement of a syndicated financing transaction shall be subject to the following core principles:

    a. the SSBs of the respective syndication participants shall specifically approve the modus-operandi of the early settlement; and

    b. the early settlement shall be made after due deliberations and communication with syndication participants and the customer and with their respective approvals as necessary; and

    c. the termination shall ensure fair treatment for the parties to the syndicated financing transaction.

Pre-exit by a syndication participant

45. A syndication participant may pre-exit from the syndicated financing transaction before its maturity as per the terms and conditions of the inter-financier agreement, duly complying with the contractual terms of the syndicated financing transaction and the relevant Shari'ah principles and rules.

46. The syndication participant intending a pre-exit shall, at a minimum, ensure compliance with the inter-financier agreement. In complying with such requirements of the inter-financier agreement, the syndication participant shall:

    a. inform the customer (and obtain its prior approval, if so required by the syndicated financing transaction agreements / inter-financier agreement for clearance) of pre-exit and replacement with an existing syndication participant or a new / incoming syndication participant;

b. inform other syndication participants through the lead arranger and / or the security agent of such decision along with the rationale for the same;

c. seek a no objection certificate (NOC) from other syndication participants, if so required by the inter-financier agreement, in a manner as specified therein;

d. sign a non-disclosure agreement (NDA) with the customer and / or other existing or incoming syndication participants, if so required by the inter-financier agreement, in a manner as specified therein.

Restructuring or rescheduling of syndicated financing transaction

47. Restructuring or rescheduling of a syndicated financing transaction may generally occur in the following scenarios:

    a. as a result of the customer's default or risk of potential default; or

    b. as a result of acquisition, merger or corporate restructuring of the customer.

48. Any restructuring or rescheduling of a syndicated financing transaction shall ensure that it is being undertaken while maintaining the primary objective of the original transaction, the initial equilibrium of financial benefits or rights and safeguarding the interests of the related parties.

49. Any restructuring or rescheduling proposition shall be thoroughly reviewed and approved by the respective SSBs of the syndication participants, the customer (if any) and, where applicable, the regulator to ensure Shari'ah compliance and safeguard the interests of the parties to the syndicated financing transaction.

Part H: Considerations at maturity of the syndicated financing transaction

The respective parties' responsibilities at maturity of the syndicated financing transaction

50. The customer, the arranger(s), the syndication participants and the security agent, in their respective areas of responsibilities, shall ensure that at the maturity of a syndicated financing transaction, the transaction conclusion process is carried out in line with the requirements of Shari'ah principles and rules and relevant contracts.

51. Where needed, the SSBs of the respective syndication participants shall supervise the process of liquidation to ensure compliance with Shari'ah principles and rules.

Effective date

52. This standard shall be effective on syndicated financing transactions executed on or after 01 July 2023. Earlier application is encouraged.

Appendices

Appendix A: Adoption of the standard

This standard was presented for the approval in the AAOIFI Governance and Ethics Board's meeting No. ____________held on ____________H, corresponding to ____________ and was duly approved.

Members of the Board

1. Mr. Mohammad Farrukh Raza (chairman)
2. Dr. Walid Hegazy (deputy chairman)
3. Dr. Abdulbari Mashal
4. Mr. Abdullah AlMoqbel
5. Mr. Abozer Magzoub
6. Dr. Ahmet AlBayrak
7. Dr. Ali Sartawi
8. Mr. Ebrahim Sidat
9. Ms. Ibtihal Al-Shamali
10. Dr. Mohammad Kabir Hassan
11. Mr. Moosa Khoory
12. Mr. Muzammil Kasbati
13. Mr. Sohaib Umar
14. Mr. Wael Merza
15. Dr. Zahid ur Rehman Khokher

Reservation

The standard was approved unanimously.

Working group and team

1. Dr. Abdulbari Mashal (chairman)
2. Dr. Ahmet AlBayrak
3. Mr. Dalip Kumar Kaul

4. Mr. Fazal Rahim
5. Mr. Ijlal Ahmed Alvi
6. Mr. Lilian Le Falher
7. Mr. Mohd Faysal Mohammed
8. Mr. Mohamad Jamali
9. Dr. Mohammad Kabir Hassan
10. Mr. Muhammad Faisal Shaikh
11. Mr. Saiful Anuar Hambali
12. Mr. Samer Odeh

Executive team

1. Mr. Omar Mustafa Ansari (AAOIFI)
2. Ms. Zahra Jassim (AAOIFI)
3. Ms. Alyaa Adel (AAOIFI)
4. Mr. Aamir Mohammad (Senior Research Associate)

Appendix B: Illustrative depiction of the syndicated financing transaction

Appendix C: Basis of conclusion

Scope of the standard: applicability on Sukuk

BC1 The board considered the matter of application of certain requirements of this standard on Sukuk transactions, as well as, the potential overlap with the guidance provided in AAOIFI GS 12 "Sukuk Governance".

BC2 In this respect, the board considered the option to either provide guidance for specific matters exclusively for syndicated financing transactions or include Sukuk issuance-related aspects (partially or fully) within the scope of the standard.

BC3 After due deliberations, the board decided that the standard should focus exclusively on syndicated financing transactions and not repeat the Sukuk governance requirements. However, the board noted that certain requirements of this standard, particularly those applicable during the initial phases of a syndicated financing transaction, may also be relevant to Sukuk issuance, and are not explicitly included in GS 12. Accordingly, it was decided to exclude Sukuk from the scope of this standard, while creating a reference to the potential requirements which may be considered as adding value for Sukuk governance.

BC4 The decision was based on the established principle of the board to avoid overlaps in the scope of the two types of transactions, duly considering that at times these transactions are subject to the jurisdiction of two different regulators i.e., the banking regulator and the securities market regulator.

Inter-financier agreement: inclusion of illustrative format in the standard

BC5 It was initially proposed and considered by the working group and the board that the standard should include more details, and potentially, an illustrative format of an inter-financier agreement. This was considered appropriate due to the significance of an inter-financier agreement in the overall context of the governance requirements set out by this standard.

BC6 The board discussed the issue at length, including the need for guidance in this aspect and the potential risk of overlap with the scope and mandate of other standard setting bodies (International Islamic Financial Market (IIFM), in particular). The board was informed that IIFM has already planned and initiated a project on the development of a documentation standard on an inter-creditor / inter-financier agreement.

BC7 After due deliberation, the board decided that the standard shall include the minimum contents for an inter-financier agreement to ensure compliance with the best practices, but not an illustrative format of the same.

The need for a common SSB and shared functions for Shari'ah compliance

BC8 The working group and the board deliberated on the proposal of establishing a common SSB for each syndicated financing transaction (either being the SSB of the lead arranger or a joint SSB comprising of nominated members from the syndication participants). The proposal also included certain shared functions for ensuring Shari'ah compliance including a periodic external Shari'ah audit of each transaction. The overall rationale supporting such proposal was improved compliance at reduced costs and efforts, as well as, smooth and timely execution of transactions.

BC9 The board, in line with the conclusion reached by the working group, decided to reject the said proposal on the grounds of being difficult to implement, entailing higher costs and administrative challenges, hence its disadvantages may surpass the advantages. In particular, the board considered that in line with the AAOIFI GSs and the regulatory frameworks in different countries, the responsibilities of the respective SSBs of individual IFIs may not be shared with others. Similarly, the selection of such transactions for external and internal Shari'ah audits will be based on the materiality and sampling approach applied by the respective auditors, which may differ from case to case.

Discouraging hybrid syndicated financing transaction

BC10 The board considered various governance and Shari'ah compliance issues that may arise in hybrid syndicated financing transactions, particularly due to the involvement of CFIs and the risk of commingling of funds. The board also considered whether IFIs shall not be allowed to participate in such transactions due to these issues. The board further considered that CFIs are not subject to the requirements of this standard, and hence compliance of the standard will become difficult in case of a CFI taking the lead.

BC11 After due deliberation, the board principally agreed that due to specific industry needs in different jurisdictions and in line with the recommendation of AAOIFI SS 24 "Syndicated Financing", a hybrid syndicated financing transaction shall not be considered preferred, and hence to be discouraged generally, but allowed while fulfilling certain specific conditions.

BC12 Besides other conditions, the board emphasised that in a hybrid syndicated financing transaction, the Shari'ah compliant tranche shall be separately identified and only IFIs can take the role of a lead arranger for such tranche. This is the only way to ensure compliance with Shari'ah principles and rules and the requirements of this standard.

Use of the term "inter-financier agreement" vs. "inter-creditor agreement"

BC13 The board discussed the most suitable term to be used to describe the agreement which details the rights and obligations of the syndication participants.

BC14 The members discussed the suitability of the term "inter-creditor agreement" (which is commonly used in the financial sector), vs. the term "inter-financier agreement" or "syndication participants' agreement" or "syndication agreement".

BC15 After due deliberation, the board rejected the term "inter-creditor agreement" to avoid similarity with the conventional transactions and in consideration of the true nature of Islamic financing transactions (which is not credit or borrowing). The board generally agreed on the acceptability of other possible terms, but in order to avoid any confusion with the transaction documents, decided to use the term “inter-financier agreement”. For additional clarity, the board also decided to include a definition of the term.

Responsibilities of the customer

BC16 It was initially proposed to specify certain responsibilities of the customer, in order to ensure Shari’ah compliance and fair and equitable treatment amongst stakeholders. One such matter discussed was that a potential customer shall not award a mandate to an arranger(s) if it is probable that such an action will result in jeopardising the interests of a party or parties of the syndicated financing transaction.

BC17 This approach was debated amongst the board members with regard to the mandate of the board and the mandate of the regulators who adopt AAOIFI standards, considering the fact that typically the customers of the syndicated financing transactions are not IFIs. It was argued that the Shari’ah compliance requirements also include the responsibilities of the customer, who is required to abide by such requirements being subject to the provisions of Shari’ah compliant contracts of financing and investment. It was further argued that AAOIFI’s mandate is not limited to IFIs but includes Islamic finance transactions as well.

BC18 Having agreed in principle that the customer’s role is important in governance of such transactions, it was decided to keep the onus of compliance of the standard on the IFIs as much as possible. It was further decided that the customer shall be required to abide by the requirements of this standard along with the requirements for complying with the Shari’ah principles and rules by virtue of signing the respective contracts and documents (including mandate, in particular).

Appendix D: Brief history of the preparation of the standard

H1 The secretariat proposed developing a standard on syndicated financing in the 20th meeting of AGEB held on 16-17 Sha'ban 1442H, corresponding to 29-30 March 2021 via video conferencing. The members agreed that there is a need in the market and approved the initiation of the project and formation of the working group.

H2 Following the board's approval, two working group meetings were held to discuss the preliminary study of the standard on 19 Dhul-Qa'dah 1442H, corresponding to 29 June 2021 via video conferencing and on 24 Dhul-Hajjah 1442H, corresponding to 3 August 2021 via video conferencing. The members discussed the preliminary study and agreed on conceptual issues. The working group approved the preliminary study.

H3 Following the approval of the preliminary study, the development process of the exposure draft started. The working group held several meetings to discuss the exposure draft. The meetings were held via video conferencing on 26 Rabi' I 1443H, corresponding to 1 November 2021, 29 Rabi' I 1443H, corresponding to 4 November 2021 and 10 Rabi' II 1443H, corresponding to 15 November 2021.

H4 AGEB held its 23rd meeting on 24-25 Rabi' II 1443H, corresponding to 29-30 November 2021 at the AAOIFI Head office in Bahrain and approved the issuance of the exposure draft. The board directed the secretariat to make the necessary changes in light of the comments of the AGEB members and the discussion during the meeting. After due process, the exposure draft was issued on 25 Jumada I 1443H, corresponding to 29 December 2021.