



**C L I F F O R D**  
**C H A N C E**

WORKSHOP ON IIFM STANDARDS

SESSION: ISLAMIC HEDGING STANDARDS

**QUDEER LATIF**

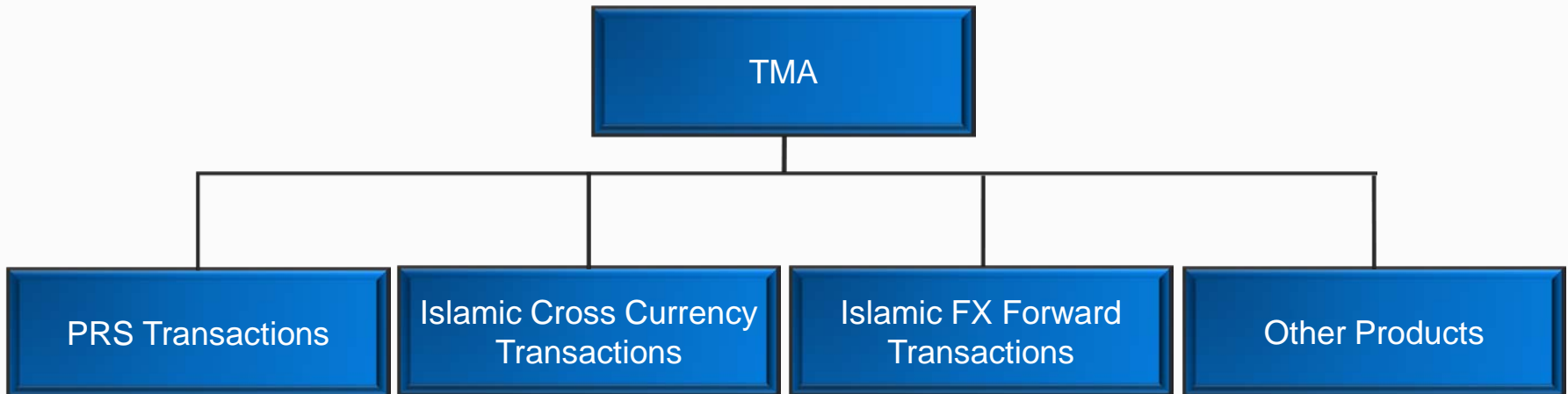
10 April 2017

# THE ISDA/IIFM TAHAWWUT MASTER AGREEMENT

# ISDA/IIFM TAHAWWUT MASTER AGREEMENT

## Architecture

- Framework Agreement
- Multiproduct Single Agreement with close-out and netting
- Products under the TMA can be collateralised through cash variation margin through the use of the new Islamic Credit Support Deed for Cash Collateral



# EXPLANATORY MEMORANDUM

## **Guidelines regarding the sorts of transaction that may be entered into under the ISDA/IIFM Tahawwut Master Agreement. For the purposes of Shari'ah compliance:**

- Transactions entered into under the ISDA/IIFM Tahawwut Master Agreement should only be for the purpose of hedging actual risks of the relevant party
- Transactions should not be entered into under the ISDA/IIFM Tahawwut Master Agreement which are for the purposes of speculation
- Transactions must be real transactions, involving the actual transfer of ownership of real assets, actual risk and real settlement
- The asset itself must be halal
- Interest must not be chargeable under the transaction

# TRANSACTIONS/DFT TERMS AGREEMENTS

## **Under the Agreement, you can enter into:**

- Transactions
- DFT Terms Agreements

# CLOSE-OUT AND NETTING - SECTION 6 - EARLY TERMINATION

## **Fully Delivered Terminated Transactions:**

- (section 6(d)): accelerate all payments due after the Early Termination Date (Close-out Amount)
- (Section 6(e)): add unpaid amounts

## **Non-Fully Delivered Terminated Transactions:**

- (section 6(e)): add unpaid amounts to Fully Delivered Transactions amount
- (section 6(f)): treat not made deliveries and future payments like a DFT Terms Agreement

# CLOSE-OUT AND NETTING - SECTION 6 - EARLY TERMINATION – DFT TERMS AGREEMENTS

- Calculate Market Quotation (or Loss) (section 6(h))
- Result may be positive or negative
- Becomes value of Relevant Index
- Index Amount means, with respect to each DFT Terms Agreement or each group of DFT Terms Agreements, the amount of the losses or costs that would be incurred or gains that would be realised in replacing, the material terms of that DFT Terms Agreement or group of DFT Terms Agreements

## SECTION 6 - EARLY TERMINATION - MUSAWAMA

- Section 6(f)(v): if Relevant Index is positive (Determining Party is in the money), Determining Party can exercise the section 2(e) wa'ad of counterparty requiring counterparty to enter into musawama and purchase asset from Determining Party at the Positive Indexed Value
- Section 6(f)(v): if Relevant Index is negative (Determining Party is out of the money) other party can exercise the section 2(e) wa'ad of the Determining Party requiring the Determining Party to purchase asset from the other party at the Negative Indexed Value
- Need for real transaction with real assets
- Supported by set off (section 6(h))
- The musawama price is expressed as a single number (actually calculated by adding cost of asset to Relevant Index Value plus applicable VAT or similar taxes)
- The type and quantity of the asset to be the subject of the musawama will be fixed and specified in the Schedule at the outset (minimises gharar)



# THE MUBADALATUL ARBAAH (PRS) DOCUMENTATION

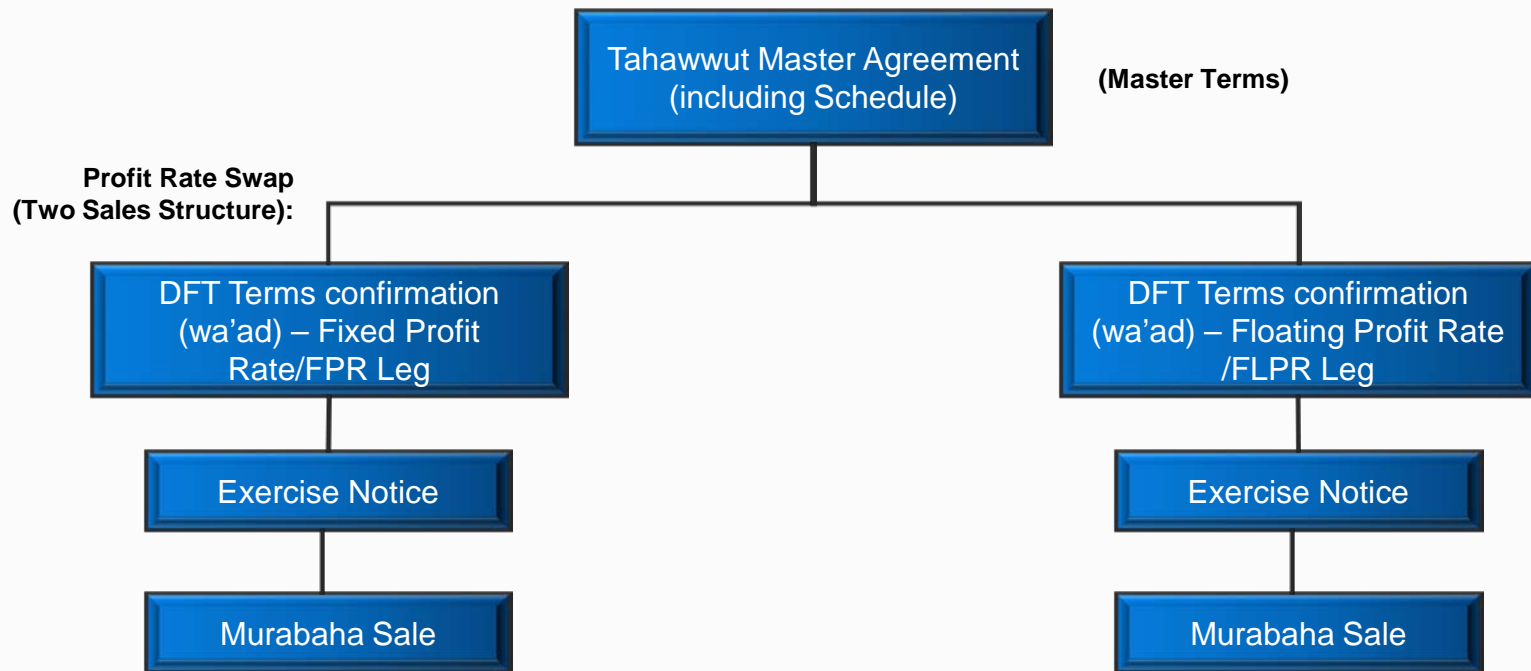
# THE MUBADALATUL ARBAAH (PRS) DOCUMENTATION

- Party A and Party B have already entered into a Tahawwut Master Agreement
- To enter into the PRS, Party A and Party B enter into two separate **DFT Term Agreements** (each of which is documented in a separate **DFT Terms confirmation**: one in respect of the fixed rate leg of the PRS and one in respect of the floating rate leg of the PRS)
- Each DFT Terms confirmation contains a wa'ad (undertaking) to enter into one or more Designated Future transactions (if the wa'ad is exercised)

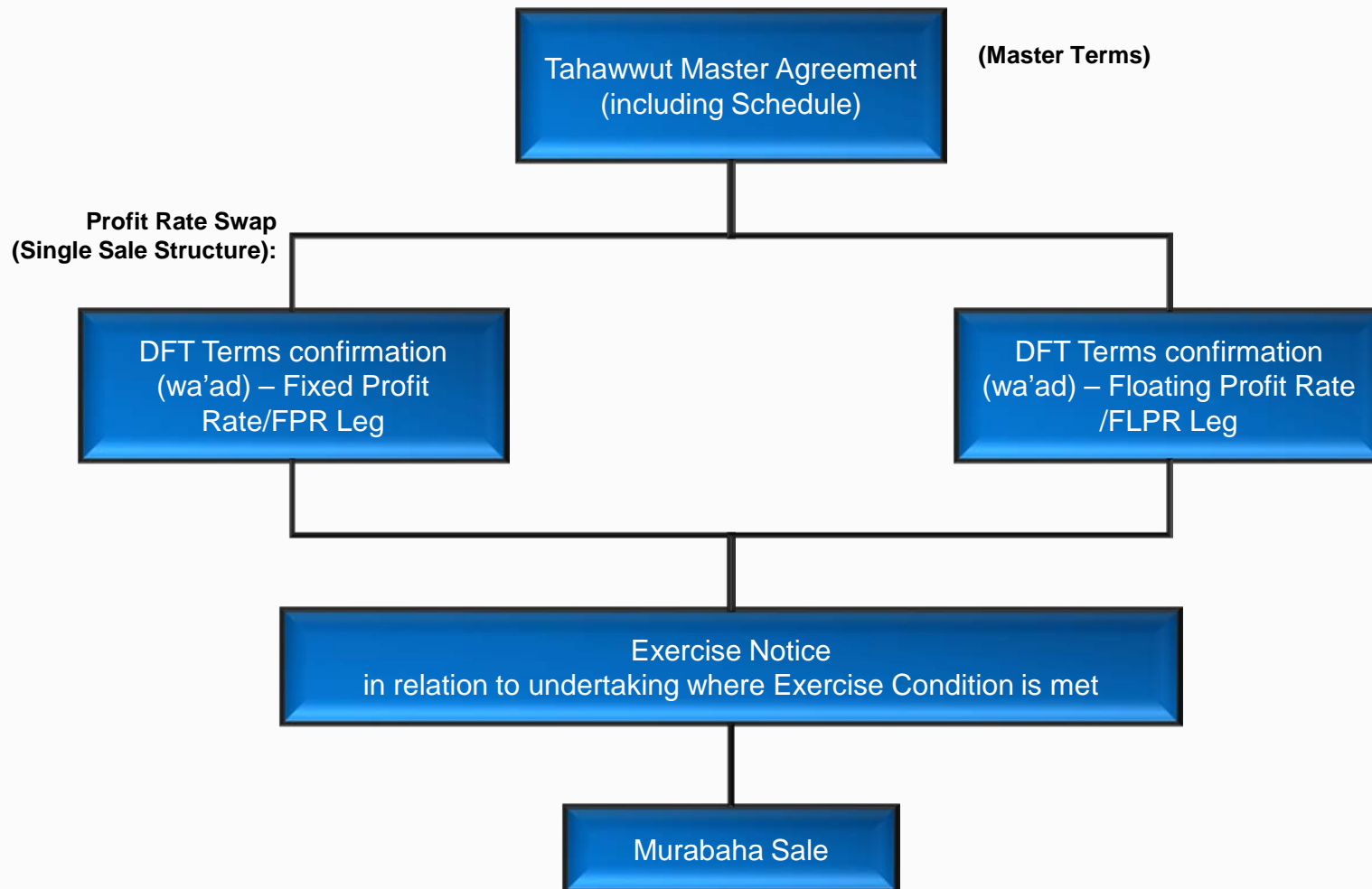
# PRS TEMPLATES - PROCESS

- Schedule
- Fixed Rate Leg DFT Terms confirmation (Wa'ad)
- Floating Rate Leg DFT Terms confirmation (Wa'ad)
- Exercise leads to
  - entry into Murahaba (Transaction Confirmation)
  - delivery of asset
  - payment (deferred or spot basis)

# TWO SALES STRUCTURE DOCUMENTATION ARCHITECTURE



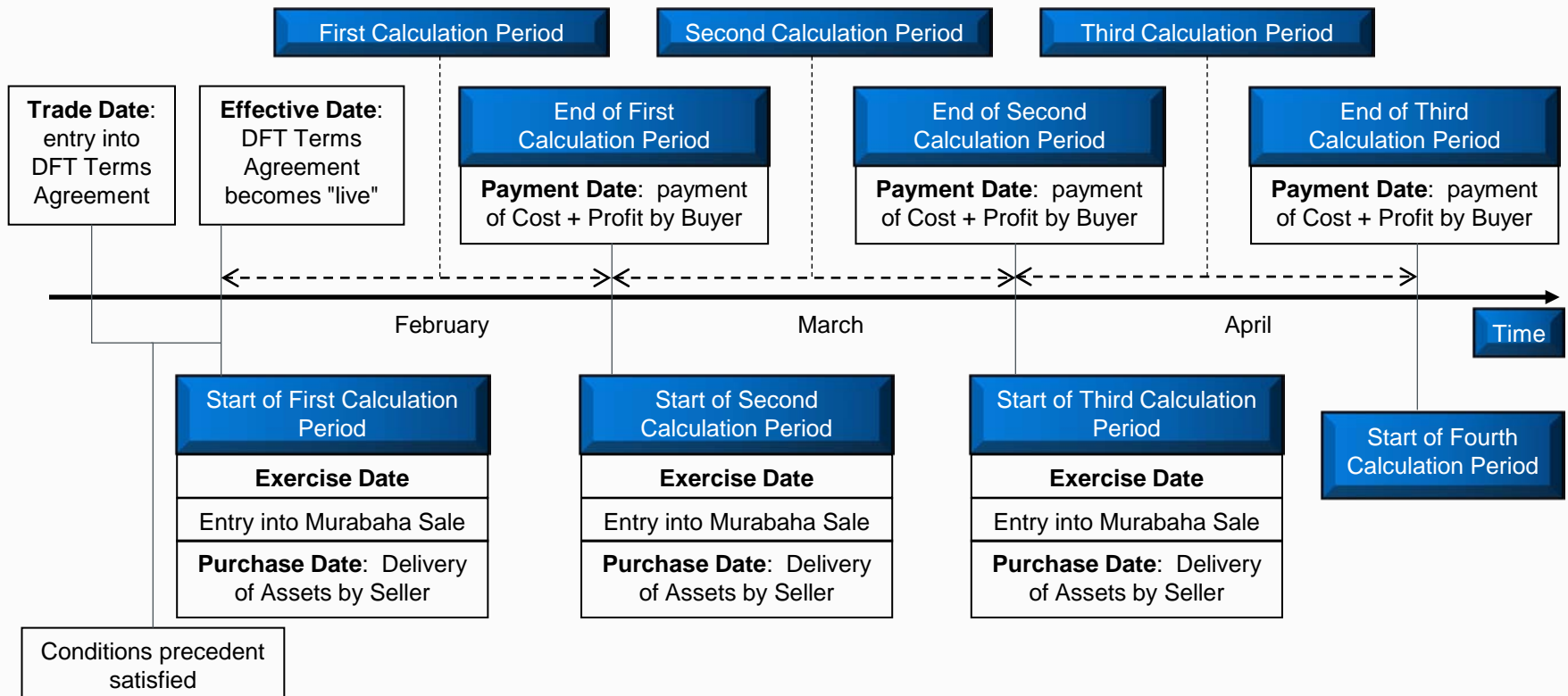
# SINGLE SALE STRUCTURE DOCUMENTATION ARCHITECTURE



# EXAMPLE TIMELINE OF ENTRY INTO MURABAHA SALE AT THE START OF EACH CALCULATION PERIOD

This diagram illustrates an example of entry into Murabaha Sale at the start of each Calculation Period:

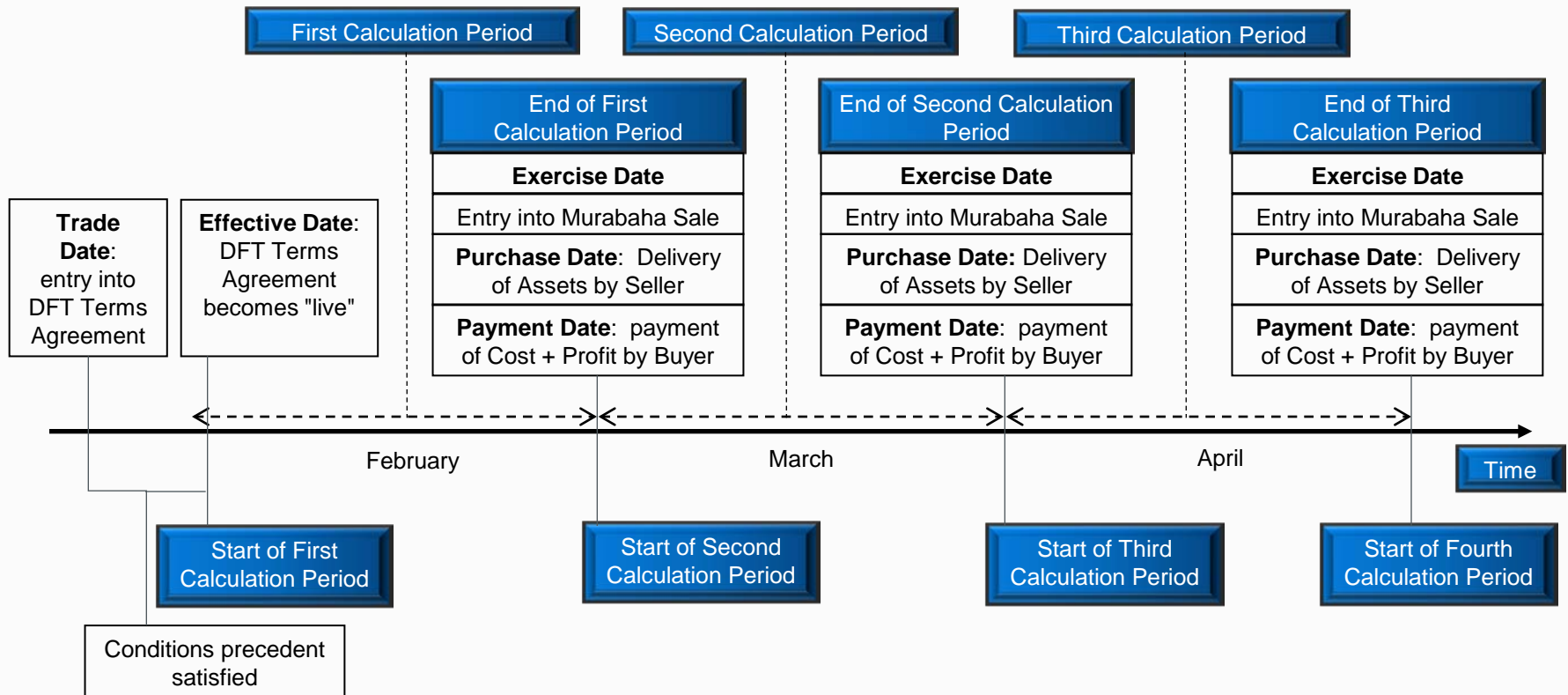
- Purchase Date at start of Calculation Period
- Payment Date at end of Calculation Period



# EXAMPLE TIMELINE OF ENTRY INTO MURABAHA SALE AT THE END OF EACH CALCULATION PERIOD

This diagram illustrates an example of entry into Murabaha Sale at the end of each Calculation Period:

- Purchase Date at start of Calculation Period
- Payment Date at end of Calculation Period



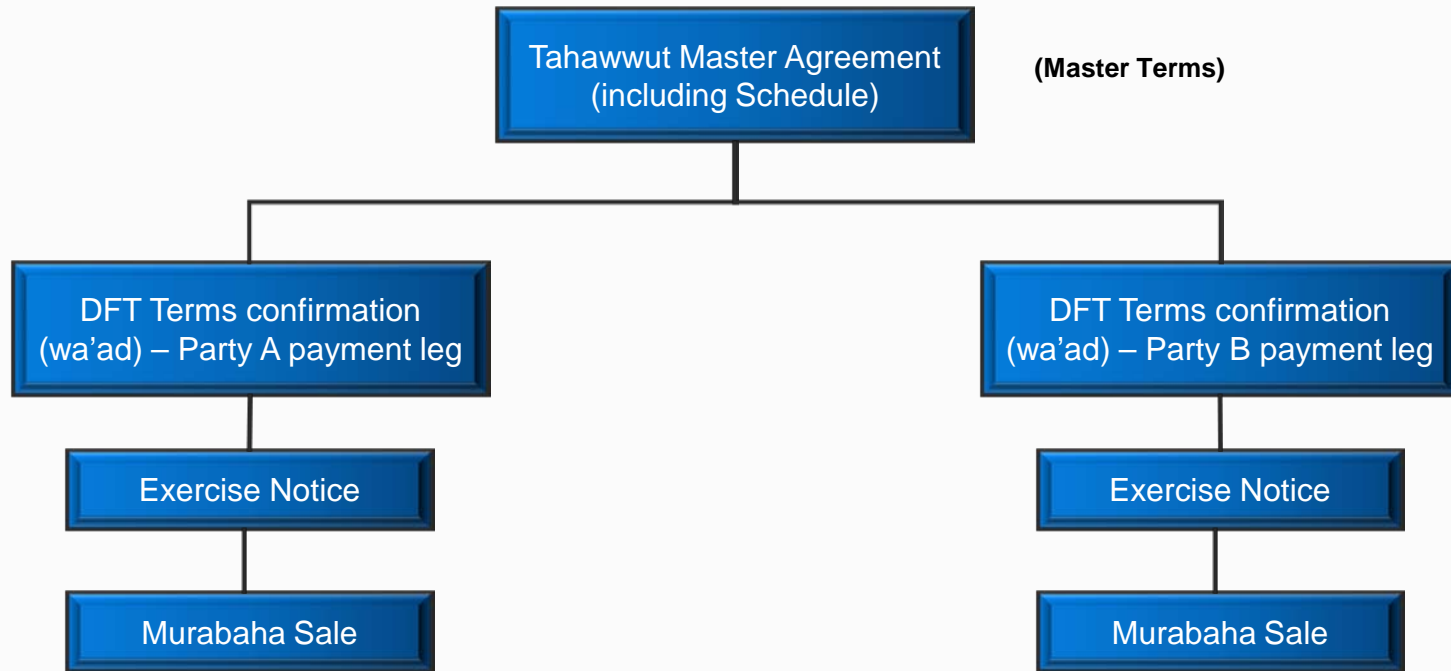
# THE HIMAAYAH MIN TAQALLUB AS'AAR ASSARF (CROSS CURRENCY SWAP) DOCUMENTATION



# ISLAMIC CROSS CURRENCY SWAP

- Similar structure to “two sales” PRS
- Wa’ad (undertaking) leading to murabaha transaction for the sale and purchase of assets
- The murabaha transactions deal with
  - Initial exchange of currency
  - Interim exchanges for profit rate – different Profit Types can be specified in DFT Terms confirmation
  - Final exchange of currency

# ISLAMIC CROSS CURRENCY SWAP DOCUMENTATION ARCHITECTURE

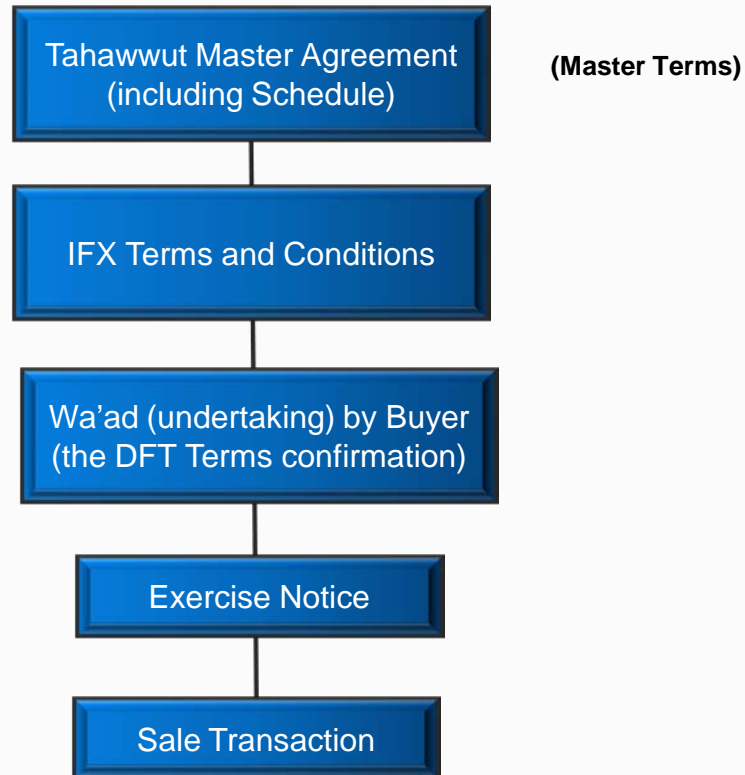


# THE WIQAYAH MIN TAQALLUB AS'AAR ASSARF (FOREIGN EXCHANGE FORWARDS) DOCUMENTATION

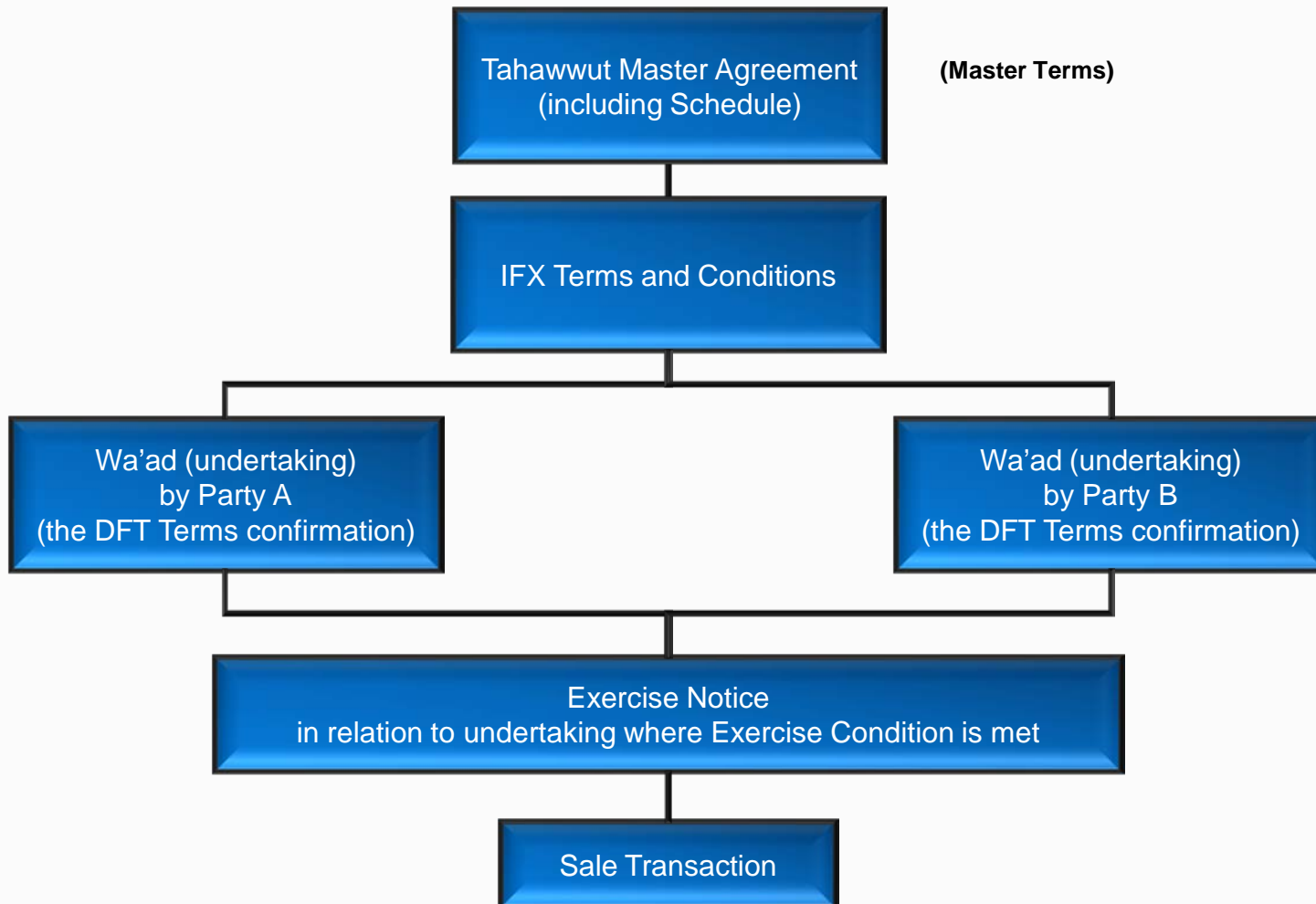
# ISLAMIC FX FORWARDS DOCUMENTATION

- Two versions of published templates available, both wa'ad-based:
  - single wa-ad structure – to reflect general usage by market participants
  - two wa'ad structure – to reflect Shari'ah preferences by some market participants
- Exercise of wa'ad leads to exchange of currencies at a pre-agreed exchange rate
- Execution of prohibited template provides a framework for future entry into IFX trades between parties

# SINGLE WA'AD STRUCTURE DOCUMENTATION ARCHITECTURE



# TWO WA'AD STRUCTURE DOCUMENTATION ARCHITECTURE



# THE ISDA/IIFM 2017 CREDIT SUPPORT DEED FOR CASH COLLATERAL (VM)

# ISDA/IIFM CREDIT SUPPORT DEED INTRODUCTION

- Published on 30 March 2017 in response to market demand for collateral document for use with TMA
- Allows parties to post cash collateral as variation margin on net exposures under trades that are designated as “Covered Items”
- Security interest (not title transfer) is created over Posted Cash Collateral: for Shari’ah reasons and lack of robust netting in some counterparty jurisdictions
- Eligible collateral is cash only
- Document facilitates collateralisation of unsecured OTC trades required under regimes such as EMIR and Dodd-Frank



# ISDA/IIFM CREDIT SUPPORT DEED KEY ELEMENTS

- **English law charge** – the security interest clause in the ICSD as an English law charging clause
  - local law considerations will apply if Posted Cash Collateral is held outside of England and Wales
  - perfection requirements will need to be considered depending on counterparties' jurisdiction
  - collateral posting and collection arrangements need to be considered
- **Variation margin calculation** – on net exposures of either party under trades or types of trades under the TMA which are designated as “Covered Items” in the Annex
  - haircuts on collateral may apply depending on currency of Eligible Collateral and if a party is in a robust netting jurisdiction
  - additional provisions need to be added if collateral needs to be collected or posted in gross exposures

# ISDA/IIFM CREDIT SUPPORT DEED KEY ELEMENTS (CONTINUED)

- **Enforcement** – if there is an early termination under the TMA, security enforcement takes place on the Posted Cash Collateral against the amounts owed by the chargor-party
- **Returns on Posted Cash Collateral** – not in ICSD, but parties can agree further arrangements to pay Investment Returns on Posted Cash Collateral

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Clifford Chance, Level 15, Burj Daman, Dubai International Financial Centre, P.O. Box 9380, Dubai, United Arab Emirates

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