

**THE MALAYSIAN SUKUK MECHANISM AS THE MOST MODERN  
FORM OF SUKUK RELATIONSHIP REGULATION.**

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Malaysia is one of the leaders in the development of Islamic financial services and is the largest sukuk market in the world. By the end of 2007, 68.9% of global sukuk, or US\$62 billion (RM213 billion), originated in Malaysia. In 2007, the total issuance of corporate sukuk in Malaysia exceeded RM30 billion. Leadership in the development of Malaysia's sukuk market is not limited to volume, but also includes the introduction of innovative and competitive sukuk structures that appeal to a wider investor base. Malaysia also has a strong and comprehensive Islamic financial system based on a stable business-oriented regulatory regime and legal framework. Malaysia has become the world's largest sukuk market, with total sukuk volume of MYR 173.5 billion as of March 2015, equivalent to 57% of the global market. The Sukuk market has become an integral part of the Malaysian capital market. Over the years, Islamic capital market products have gained global acceptance as an alternative to conventional products. There is clear evidence of acceptance of these products by non-Muslim issuers and investors. As evidence of Malaysia's success in the Islamic capital market, 35% of all ringgit bond issuances (MYR62 billion) in 2014 were through sukuk.

**Stages of development of the sukuk market in Malaysia.**

In Malaysia, due to the increase in the population, the development of financial services and the increasing use of financial services by the population, the rapid growth of the economy, the increase in the need to invest capital in production processes, especially the improvement of religious literacy among the population, which is in accordance with Islamic Sharia. The growing demand for Islamic financial services, especially sukuk, as an alternative to conventional financial services, has prompted the government to take concrete steps in this regard. It also set himself the goal of modernizing the Malaysian economy and financial system, bringing it to the international level. This made the development of Islamic finance services an urgent issue for the government.

**The first stage is the creation of the Islamic financial system and the introduction of sukuk (1980-1990s).**

The beginning of this period is associated with the creation of the first Islamic banking law in Malaysia, the Islamic Banking Act, in 1983. The adoption of this law is the legal basis for the operation of Islamic financial services in the country. created and introduced rules clearly regulating the activities of Islamic banks and other financial institutions. The creation of this law led to the establishment of Bank Islam Malaysia Berhad (BIMB) in 1983, a Malaysian Islamic bank. This bank is the first Islamic bank in Malaysia, and its opening was a programmatic step in the introduction of Islamic financial services in the country. When introducing the Islamic finance system, the first reason for opening an Islamic bank was that the population did not want to use financial services based on interest and wanted to establish banks and financial institutions that conform to Islamic Sharia, and the next reason is that such Islamic institutions help to differentiate the country's financial services and compare with other Muslim countries. was to strengthen financial and economic integration.

Thus, the adoption of the "Securities Commission Act 1983" adopted in 1983 led to the legal regulation and development of the national capital market. The main purpose of this law was to increase the reliability and transparency of the stock market, protect the rights and interests of local and foreign investors, ensure and control the efficient operation of the stock market.

Through this law, the activity of the Securities Commission, which controls the securities market, was established. The main task of the Securities Commission is to control all operations in the capital market, its main tasks are to determine the laws and regulations regulating the activity of securities in the country's financial market, to protect the rights of investors, to prevent various frauds against them, to introduce new financial introduction of products, making the national financial market competitive, ensuring its stability in the global financial markets.

Thus, the Securities Act has served as a key legal instrument in ensuring the efficient functioning of the Malaysian financial market, protecting investors and making the market internationally competitive.

The establishment of an Islamic bank directly motivated the introduction of Islamic securities in the country. For example, in 1990, Shell MDS Sdn Bhd company issued sukuk securities for the first time. It was the first Islamic financial instrument issued in the corporate sector in Malaysia. This sukuk was issued on the principle of lease and greatly helped to finance the necessary infrastructural projects. Originally, the sukuk issued were based on Islamic contracts such as ijara (lease contracts) and murabaha (sales contracts).

**The second stage is the development of the sukuk market (1990s-2010s).**

This period is characterized by the rapid development of sukuk, making Malaysia the center of the sukuk financial instrument in the Islamic financial services

industry. In particular, regulatory documents regulating murabahah, musharakah, exclusion and rental sukuk relations were developed in accordance with Sharia requirements. The beginning of this period is directly related to the adoption of the Securities Commission Act of 1993. This Act is considered one of the main pieces of legislation developed to regulate the securities market in Malaysia, through which the Securities Commission Malaysia (SC) was established. This commission is entrusted with a wide range of tasks aimed at ensuring the development, transparency and stability of the securities market in Malaysia. , protecting the interests of investors, as well as comprehensively developing the sukuk Islamic instrument in the stock market. As for its powers, it consists of registering and approving new securities, auditing the activities of market participants and their licensing, taking measures against market manipulation and fraud, and strategically managing the development of the market of Islamic financial products.

In 1994, the Law "Islamic Banking Act" was adopted. This law made it possible to expand sukuk activities by implementing the system of regulatory documents regulating the activities of Islamic financial institutions in Malaysia. In particular, Islamic banks and other Islamic financial institutions were given the right to develop and use financial instruments such as sukuk. This prompted Islamic banks to develop Islamic securities adapted to the capital market. At the same time, through this law, the powers of the council considering Sharia issues were determined, and this became important in considering the Sharia compliance of sukuk projects and contracts.

In 2002, the first international sovereign sukuk (Islamic government-issued securities) was issued, which was one of the important steps for the development of the global Islamic financial system, not only for Malaysia, but also for the entire world of Islamic finance. This sovereign sukuk is a leased sukuk, issued by the Malaysian Treasury (Ministry of Finance, Malaysia) for a period of 5 years in the amount of 600 million US dollars.

The issuance of this international sovereign sukuk is the first Islamic security for international investors, which has demonstrated the potential of Islamic finance internationally and opened a new direction in the world of Islamic finance, such as international Islamic financial instruments. This led to the recognition of Malaysia as a major international player in sukuk. This issued sukuk attracted investors from many Arab, European and Asian countries and popularized international sukuk issuance by state organizations and private companies in this country. Also, the proceeds from the sukuk issue were used to finance large infrastructure projects, which increased the country's financial stability and made a significant contribution to the diversification of public debt.

In 2004, the Securities Commission of Malaysia issued the Guidelines on the Offering of Islamic Securities, a special guideline for the issuance and supervision of sukuk, which helped to standardize sukuk structures in accordance with Shariah

principles. . After that, in 2006, with the efforts of the country's government, the "Islamic Financial Services Board" (IFSB) was established. This is certainly one of the most important steps in the world of Islamic finance, and this council has become an important institution that sets standards in the field of Islamic finance at the international level.

Also, by this time, the Capital Markets and Services Act was passed in 2007 in order to create more flow of investors to finance many projects, increase competitiveness in order to maintain the main playing position in the sukuk market, and further expand the sukuk market. Act) was adopted. This especially made the trading of sukuk financial instrument in the secondary markets easier, making it easier for investors to buy and sell sukuk, which in itself increased the liquidity of sukuk.

Legal problems and their solutions arising in the introduction of sukuk mechanism.

The first legal problem that arose in the creation of the sukuk mechanism in Malaysia was the legal separation between traditional bonds and sukuk. At the same time, it was necessary to issue sukuk in accordance with Sharia requirements, to separate them from prohibitions prohibited by Sharia, for example, interest practices. In general, there is a problem of monitoring compliance with the prescribed sharia laws of any entity that implements sukuk activity. This is because the lack of general and specific Shari'ah oversight is compounded by the country's numerous Sharia prohibitions on issuing local and international sukuk financial instruments, which may increase uncertainty about sukuk and undermine Malaysia's efforts to introduce a sukuk mechanism. Therefore, a strong control body over compliance with Sharia requirements for sukuk activities in the country was necessary. For this reason, the Securities Commission and Bank Negara Malaysia (Central Bank) have started promoting initiatives aimed at establishing Sharia Councils. By 1996, the first formal Shariah Board was established by Bank Negara Malaysia and the Securities and Exchange Commission. The most important legal documents regulating the activities of the Sharia Council are the Securities Commission Act (SCA) and the Islamic Financial Services Act. The main task of this council is to verify the compliance of Islamic financial services with the requirements of Shariah, to provide solutions and advice on problems related to Islamic financial services, and to conduct various scientific studies on the creation of financial products that comply with Shariah principles.

In general, there is a central Shariah advisory board and Shariah advisory councils established within Islamic financial institutions to oversee Islamic financial services, particularly sukuk financial instruments. Shariah advisory councils established within Islamic financial institutions operate independently from the SAC and are not directly subordinate to it. So, it can be seen that there are two layers of independent Shariat Advisory Councils in Malaysia. However, SAC is the only

formal and centralized Shariah Advisory Board in Malaysia, whose decisions affect all Islamic financial services.

Determining the legal status of sukuk and bonds.

One of the first problems that arose when setting up sukuk was determining the legal status of sukuk. The reason is that sukuk are similar to bonds, so in practice, sukuk are widely used under the names of Islamic bonds or sukuk bonds. We know that a bond is a debt relationship and works on the basis of interest (riba). This type of activity is strictly prohibited according to the principles of Islamic Sharia. Sukuk is asset-based and does not reflect interest (riba) relationships. In Malaysia, the use of sukuk as an Islamic bond or sukuk bonds could create a risk of not being in accordance with the principles of Islamic finance. Also, such an approach to sukuk can misrepresent or obscure the true nature of sukuk, treating it as a bond.

In international financial markets, especially in European financial markets, sukuk is usually equated to a bond. Therefore, naming sukuk as an Islamic bond or sukuk bond makes it easier for foreign investors to understand. However, this could lead to the problems mentioned above.

Various scholars, Shariah advisory councils, and other financial institutions have had heated debates on this matter in Malaysia. The most important task before them was to preserve the original nature of sukuk while fully complying with Sharia requirements, and at the same time to achieve easy acceptance of sukuk in international financial markets.

The Shariat Advisory Councils have also taken important steps in this regard. First of all, guidelines for sukuk were developed in accordance with Sharia requirements. One of them is "Shariah Parameters on Sukuk" (Shariah Parameters on Sukuk).

Another guideline is the "Guidelines on Sukuk" (Guidelines on Sukuk), developed by the Securities Commission of Malaysia (SC). This instruction contains all the rules for sukuk issuance. The guidelines include the terms of issuance of sukuk, terms of contracts for types of sukuk, Sharia requirements and their application.

The second issued guideline is "Guidelines on Issuance of Corporate Bonds and Sukuk to Retail Investors" (Guidelines on Issuance of Corporate Bonds and Sukuk to Retail Investors), in paragraph 2.01 of this guideline, sukuk is clearly defined:

"Certificates of equal value evidencing undivided ownership or investment in property based on ahari'ah principles approved by the Shari'ah Advisory Council (SAC)."

This guideline also clearly defines a bond:

"Bond" means debentures, notes or other debt instruments evidencing or acknowledging indebtedness and includes Islamic securities but does not include structured products."

It can be seen that sukuk and bond are clearly distinguished. At the same time, "Tax Incentives and Guidelines on Sukuk Issuance" (Tax Incentives and Guidelines on Sukuk Issuance), which includes the necessary guidelines for sukuk issued in foreign currency and tax incentives for issuing sukuk Sukuk Issuance), as well as the "Sustainable and Responsible Investment (SRI)" which sets out procedures for issuing sukuk for projects aimed at supporting social and environmental sectors guidelines" (Guidelines on Sustainable and Responsible Investment (SRI)) were adopted.

In addition, the "Capital Markets and Services" Law, adopted in 2007, contains a number of norms that distinguish between sukuk and bonds. However, although sukuk is not defined separately, it is included in Islamic securities. Section 2 of the law defines a bond as follows:

"Bond" means debentures, notes or other debt securities evidencing or acknowledging indebtedness, including Islamic securities but excluding structured products.

As can be seen from the above, the legal status of sukuk and bonds in Malaysia is clearly defined separately, and each of them is issued in separate procedures. Under Malaysian law, a sukuk is interest-free and asset-based, while a bond is considered a debt product.

Secondary market trading of sukuk.

One of the problems that arise in the secondary market trading of sukuk is compliance with Sharia requirements. The reason is that only asset-based sukuk types can be traded in the secondary markets, and trading of debt-based sukuk types in the secondary market is prohibited according to Sharia rules. However, debt-based types of sukuk in Malaysia also had the risk of being traded in secondary markets. In addition, the mechanism of obtaining complete and detailed information about the asset and familiarization with the necessary legal documents during the sukuk trade in the secondary markets is complicated, and sometimes the buyers could not get complete information.

In order to prevent such problems, several laws and decrees have been issued. In particular, the above-mentioned Law "On Capital Markets and Services" of 2007. Through this law, sukuk issuance and trading relations in the secondary markets, as well as the procedures for their registration, are determined. Sections 58-61 of this Act provide for licensing provisions, requiring all entities engaged in sukuk trading, such as brokers and dealers, to obtain a license from the Securities Commission Malaysia (SC). this commission ensures that the activities of intermediaries are in accordance with Sharia. A similar rule is specified in Article 212.

Article 111 specifies how a person with a capital market services license should manage funds from trust accounts. must be paid to the relevant person or according to their instructions within the specified period. If a licensee violates these rules, he or she faces hefty fines or even prison terms. As can be seen from this article, it

ensures that funds from trust accounts are used only for specific and legitimate purposes, and penalties are imposed on those who make mistakes in this process.

Article 113 establishes strict rules for the management of funds in the trust account, ensuring their safety and preventing misuse, according to which Capital Market Services is licensed. A person can use funds in a trust account only in three specially defined cases:

Payment to a person or according to his instructions: Funds are withdrawn only to their actual owner or according to his written instructions;

Fee for tools: Use of these funds to cover brokerage services and other related costs;

Used in other cases permitted by law. These rules are aimed at preventing the use of funds for illegal or improper purposes. Trading of sukuk in international markets.

One of the goals of the Malaysian government in terms of Islamic financial services was to become the world leader in sukuk. For this, first of all, it was necessary to issue sukuk to the international markets and attract a large number of investors. This required the creation of a legal system in Malaysia that conforms to international laws and norms. After the first international sukuk was issued by the Malaysian government in 2002, it became necessary to develop legal regulations for the use of sukuk in international markets.

The adoption of the above-mentioned Law on Capital Markets and Services in 2007 created a legal basis for the trading of sukuk in international markets.

For example, Article 92A of this law stipulates the procedures for providing necessary and transparent information to persons who want to invest in sukuk capital market products. can determine the essence and size. This request should include the following information:

- a. information explaining the main features of the capital market product;
- b. information explaining the nature of the obligations imposed on the parties participating in the capital market product;
- c. information describing the risks associated with the capital market product;
- d. detailed information showing the important terms of the capital market product.

Any person who has:

- a. provides false or misleading information;
- b. makes a false or misleading statement; or
- c. intentionally omits to state any matter or thing that would materially misrepresent the statement or information;

shall be deemed to have committed an offense against a person who invests in capital market products and shall, on conviction, be liable to a fine not exceeding three million ringgit, to imprisonment for a term not exceeding ten years, or to both.

It is clear from this that the above norm will increase the confidence of investors, provide them with the necessary information and transparently show what their funds are spent on. It also reduces the risk of investors falling prey to fraud by limiting the provision of misleading information.

In addition, Section 5 of the law is aimed at protecting the rights of clients, and the tasks that the Securities Commission can use to protect clients in certain cases are provided. The main purpose of the norms contained in this section is to limit inappropriate management of clients' assets, to reduce possible financial risks, to ensure the stable functioning of financial markets and, most importantly, to protect investors from various frauds.

Also, the Commission may freeze assets when the subjects of this legislation do not comply with the established procedures, when they do not manage their property and assets within the framework of the established requirements, when there are cases of negative impact on the stability of the market through various frauds and manipulations, and when other illegal financial activities are detected. or impose restrictions within a certain limit, temporarily suspend or revoke the license of a licensed organization or person, the Commission audits the accounts and activities of the organization or person, or may conduct inspections and restrict non-compliant organizations from making payments to clients or third parties, as well as temporarily suspend trading in markets where speculative or risky activity is detected.

The above norms included in this section are directly aimed at protecting the rights and interests of investors, and it is intended to be implemented by preventing financial frauds and maintaining the stability of the financial system. Analyzing the above efforts, we can see that the following factors have played an important role in the rapid and comprehensive development of sukuk in Malaysia.

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