

FIM Partners

AAOIFI Shariah Standard No. 62

Redefining Sukuk Structures for Authentic Islamic Finance

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Executive Summary

AAOIFI Shariah Standard No. 62 is poised to be a transformative regulatory milestone in the Islamic finance industry. This standard aims to reinforce the Shariah authenticity of sukuk by emphasizing true asset ownership, genuine risk-sharing, and enhanced transparency. Its adoption is expected to fundamentally reshape sukuk issuance practices, particularly impacting equity-based and debt-like structures that have relied on guarantees or symbolic asset transfers. This white paper explores the motivations, requirements, implications, and anticipated market impact of Standard 62, highlighting both the opportunities and challenges ahead.

Introduction

The global sukuk market is nearing the US \$1 trillion mark, driven by its appeal as a resilient, diversified, and increasingly liquid asset class. As the market matures, it also faces new challenges including the evolution of regulatory and Shariah standards.

The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), a cornerstone of Islamic financial governance, is reaffirming the foundational Shariah principles of risk-sharing, asset-backing, and ethical finance through Standard 62. While previous standards have encouraged these ideals, the new standard goes further in ensuring legal and financial alignment between sukuk documentation and their Shariah intent.

Standard 62 represents a potential major shift in sukuk structuring practices. The Standard aims to enhance Shariah authenticity through true asset ownership, genuine risk-sharing and greater transparency.

Objectives and Scope of Standard 62

The new standard is intended to:

- **Strengthen Shariah Compliance:** By prohibiting practices that resemble conventional lending
- **Promote True Legal Ownership:** Sukuk holders must hold full legal title—not merely beneficial ownership—of the underlying assets
- **Align Risk and Return:** Especially in equity-based sukuk like Mudaraba and Musharaka, returns must reflect real asset performance
- **Enhance Transparency:** Clear asset identification and periodic disclosures are mandated
- **Clarify Legal and Accounting Treatment:** The standard requires asset transfers to be reflected on financial statements and mandates segregated accounting by SPVs
- **Reinforce Shariah Governance:** Fatwas must be embedded in documentation, and sukuk that breach thresholds may face delisting

Key Provisions of AAOIFI Standard 62

- **True Legal Ownership:** Sukuk holders must have actual legal ownership of the underlying assets — not just beneficial or nominal rights. The rights must include traceable and identified asset ownership as well as the ability to sell, lease or transfer as well as the assumption of associated risks and rewards
- **Risk and Return Alignment:** There must be an assumption of associated risks and rewards and returns must be linked to asset performance. Fixed or guaranteed returns are prohibited in equity-based sukuk (e.g., Mudaraba, Musharaka). Instruments based

on risk-sharing must avoid fixed or guaranteed returns, exclude purchase undertakings at par and avoid any implied guarantees from originators or agents (wakil)

- **Asset Transparency:** Underlying assets must be clearly identified, with periodic performance disclosures to investors
- **Accounting & Legal Clarity:** Asset transfers must be reflected in the originator's financials. SPVs must maintain segregated accounts
- **Shariah Governance:** Fatwas must be embedded in legal documentation. Sukuk breaching Shariah thresholds may be delisted
- **No Guarantees or Embedded Promises:** Principal or profit guarantees are not allowed in equity-based sukuk. Purchase undertakings must be independent contracts

Impact on Existing Sukuk Structures

Certain popular sukuk structures will need to be re-evaluated or redesigned:

- **Wakala Sukuk:** Commonly include return guarantees and repurchase undertakings. These will violate Standard 62 unless repurposed. Under the standard, wakil (agent) cannot guarantee principal or returns
- **Mudaraba Sukuk:** These are equity-based and must reflect true entrepreneurial risk-sharing. Guarantees by the Mudarib are disallowed and profit must be tied to actual performance of the Mudaraba assets
- **Musharaka Sukuk:** Require genuine joint ownership and profit/loss sharing. Fixed returns or capital guarantees are not permissible and the sukuk must reflect actual profit/loss sharing
- **Asset-Based Sukuk:** Many current sukuk are "asset based" rather than "asset-backed" meaning legal title remains with the originator. Merely using assets as references without transferring legal title will no longer suffice.

Jurisdictional Implementation Considerations

Legal systems vary in how asset ownership is recognized and transferred. This creates practical challenges for cross-border sukuk. While jurisdictions like the UAE, Bahrain, and Pakistan mandate AAOIFI compliance (compliance is required for Islamic financial institutions), others such as Saudi Arabia and Malaysia permit voluntary adoption (allowing institutions to align with AAOIFI as a benchmark for best practice. Non-Muslim-majority jurisdictions like the UK, France and South Africa have also recognized AAOIFI standards, enhancing the credibility and global

appeal of the framework. Supranational bodies like the Islamic Development Bank (IsDB) have also mandated AAOIFI compliance across their operations.

Given this growing momentum across both regulatory and institutional levels, it is reasonable to conclude that broader adoption of AAOIFI standards—particularly Standard 62—is not just likely, but inevitable.

Market Implications

Prior to Standard 62 implementation, investors bore mostly issuer credit risk whereas after implantation the risk would shift to underlying asset performance, especially for equity-based sukuk. As such, traditional correlation between sukuk and conventional bonds may weaken and credit ratings may change and would entail significant analysis of sukuk documentation to ascertain new ratings.

Short-term market risks could include a potential slowdown in issuance, especially among sovereigns and corporates, due to structural redesign needs and increased legal complexities, legal barriers in sovereign sukuk markets and a resistance from investors who are used to fixed return models. Jurisdictional divergence in implementation will also need to be overcome.

The market will adapt but, this time, adaptation will require deeper structural and philosophical alignment, not just from a legal standpoint. There are opportunities in the medium to long term, however, including greater investor confidence coupled with stronger sharia compliance as well opportunities for innovation in asset-backed structures.

Regulatory and Institutional Coordination

A consistent, global implementation of Standard 62 will require collaboration among all market participants to avoid market fragmentation. This will entail regulators working to harmonize legal frameworks and enforce compliance while Shariah Boards will need to continue to standardize fatwas and interpretations thereof. Market participants will need redesign structures and educate stakeholders while investors will need to adjust risk expectations and understand structural shifts. All in all, communication among all counterparties will be key for a successful implementation to ensure the sukuk market continues to flourish.

Timeline and Transition

The final publication of the Standard was expected to be by the end of 2025 but has since been extended to the beginning of 2026. A transition period of up to 3 years (2026–2027 anticipated as adjustment phase) is expected to be provided in order for compliance to be achieved. An

important point to note is that there will be no retrospective effect and as such, existing sukuk structures will not be invalidated.

Conclusion

AAOIFI Standard 62 represents more than a compliance update—it marks a philosophical return to the ethical core of Islamic finance. As sukuk evolve into instruments of genuine ownership and shared risk, stakeholders must embrace transparency, innovation, and collaboration.

Past transitions, such as Standard 59 (which introduced stricter tangibility ratios and dissolution triggers) and 2008 AAOIFI clarifications, show the sukuk market's resilience. These caused temporary dips in issuance but ultimately led to more robust structures. However, Standard 62's emphasis on substance over form may trigger a deeper recalibration with 2026-2027 expected to be a transition time after which we expect to see stabilization.

This potentially major shift raises important questions around structure, risk, and market readiness. While there's still a degree of uncertainty in how the standard will be interpreted and implemented, one thing is clear: the sukuk market continues to evolve. It's a market that has seen many changes whether they be from a regulatory standpoint or structural standpoint and it's a market that has adjusted to these and taken these in its stride - we expect it to continue to do so.

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