14th Meeting of the Advisory Expert Group on National Accounts,
5-9 October 2020, Virtual Meeting

Agenda item: BD1

Islamic Finance in the National Accounts and External Sector Statistics

Introduction

This information note presents the work programme of the Intersecretariat Working Group on National Accounts (ISWGNA)/Committee on Balance of Payments Statistics (BOPCOM) joint task team on Islamic finance (IFTT) to develop consistent guidance on the statistical sectorization of Islamic financial corporations and the treatment of Islamic finance transactions, flows and stocks in the national accounts and external sector statistics. The IFTT replaces the ISWGNA task force (TF) on Islamic finance which was formed in 2017 to develop guidance on the statistical treatment of Islamic finance transactions and flows in the national accounts. When developing its recommendations, the IFTT will use as its starting point the recommendations which were developed by the TF in the context of national accounts and the comments received during a consultation of the Advisory Expert Group on National Accounts (AEG) and the TF in November 2019. The IFTT will present its recommendations in a guidance note for endorsement at the AEG and BOPCOM meetings in 2021.

A paper on: Islamic Finance in the National Accounts and External Sector Statistics

For information: The AEG is invited to: Take note of the information note.

Islamic Finance in the National Accounts and External Sector Statistics

I. Background

1. **Islamic finance does not operate in the same way as conventional finance as it follows Shari'ah (Islamic law) principles and rules.** Shari'ah does not permit the receipt and payment of "riba" (one form of which is interest), "gharar" (such as excessive uncertainty, asymmetry of information and moral hazard), "maysir" (gambling), and impermissible types of sales (including, short sales) or financing activities that it considers harmful to society. Instead, the parties must share the risks and rewards of a business transaction and the transaction should have a real economic purpose and should be free of any impermissible elements or set-ups including in addition to the above, undue speculation, and exploitation of either party, among others.

2. **The 10th meeting of the Advisory Expert Group on National Accounts (AEG) discussed the implications of the implementation of the *System of National Accounts 2008 (2008 SNA)* recommendations for Islamic banking.** The AEG noted the difference in the business arrangements between Islamic banking and conventional banking and recognized the systemic importance of Islamic banking for some economies and their relative rapid growth. It further agreed that further research on the statistical implications of Islamic banking in the national accounts is required and that practical guidance on the treatment of Islamic banking transactions needs to be developed. Consequently, the Statistics Division of the Economic Commission for Western Asia (ESCWA) and United Nations Statistics Division (UNSD) created a task force (TF) on Islamic finance under the auspices of the Intersecretariat Working Group on National Accounts (ISWGNA) to address the statistical treatment of Islamic finance in the national accounts.

3. **A working group of the Islamic finance TF subsequently used current statistical standards to develop recommendations on the classification of Islamic financial instruments and corresponding property income, sectorization of Islamic financial corporations and methods to calculate the output of Islamic financial services.** These recommendations have been endorsed by the TF and AEG. However, as elaborated in this paper, two key issues still require further discussion: (i) the recommendation to classify as interest the property income for those Islamic financial instruments that are classified as deposits, loans and debt securities - this appears to be in conflict with Shari'ah law; and (ii) the method to calculate the financial intermediation services indirectly measured (FISIM) for those Islamic financial corporations which are allocated to the deposit-taking corporations except the central bank subsector (S122).

4. **A consultation of the AEG and TF on the proposals to resolve these two issues was organized in 2019 and the outcome of the consultation is presented in this paper.**

5. **Since the consultation, the United Nations Statistical Commission requested the ISWGNA to prepare a roadmap to update the System of National Accounts at its 51st**

session in March 2020. At around the same time, the IMF Committee on Balance of Payments Statistics (BOPCOM) also decided to launch a parallel process to update the sixth edition of the *Balance of Payments and International Investment Position Manual*, (*BPM6*). The BOPCOM also recognized the need for guidance on the statistical treatment of Islamic finance in external sector statistics. Thus, the ISWGNA and BOPCOM have formed a joint task team on Islamic finance (IFTT) to develop a guidance note on the consistent treatment of Islamic finance in the national accounts and external sector statistics. The IFTT, comprising experts in national accounts and balance of payments, replaces the ISWGNA task force on Islamic finance. The IFTT is co-chaired by a national accounts expert from the State of Palestine and an external sector statistics expert from Morocco. Annex 1 presents the terms of reference of the IFTT, while annex 2 shows the current list of its members.

6. Section II of this paper presents the outcome of the work of the ISWGNA TF on the classification of Islamic financial instruments and their property income, sectorization of Islamic financial corporations and the methods to calculate their output. Section III summarizes the comments which were received during the consultation on the classification of the property income associated with Islamic financial instruments which are classified as deposits, loans and debt securities and the calculation of FISIM. Section IV provides an overview of the work programme of the IFTT.

II. Classification, sectorization and calculation of output

7. **An Islamic finance task force working group on sectorization and classification developed matrices presenting draft recommendations on the classification of Islamic financial instruments and their corresponding property income, sectorization of Islamic financial corporations and the methods to calculate the output of Islamic financial services based on current statistical standards.** It also developed diagrams to show the flows between Islamic financial corporations and their clients for various Islamic financial instruments to help better understand how to record these flows in the national accounts. Participants at a workshop on Islamic Finance in the National Accounts in 2018 agreed with the recommendations, except for the two issues which are described in paragraph three.

8. **On the first issue, they noted that more research should be carried out on how to address the proposed classification, considering the prohibition of interest by Shari'ah. On the second issue, more work was required on how the property income associated with Islamic financial instruments which are classified as deposits and loans can be used in the FISIM formula.** This would heavily depend on the resolution of the first issue regarding the classification of the property income. Also, a number of countries which have both Islamic and conventional financial activities were found to be using two reference rates (one for conventional FISIM and another for Islamic FISIM) to calculate the FISIM on loans and deposits which are denominated in the same currency versus a single reference rate as implied in paragraph 6.166 and A3.25 of the *2008 SNA*, Thus, there was a need to evaluate the two methods.

9. **Annex 3 presents a description of Islamic financial instruments; how they are classified in the International Monetary Fund's (IMF) *Monetary and Financial Statistics Manual and Compilation Guide* (*MFSMCG*)[1]; the type of return payable to the asset holder; and the proposed classification of the return in the SNA.** The non-insurance financial instruments are further divided into the sources of funds and uses of funds from the perspective of the Islamic financial corporations. The diagrams which show how to record the flows between Islamic financial corporations and their clients in the national accounts for various Islamic financial instruments are presented in annex 4. The sector classification of Islamic financial corporations is presented in annex 5, together with generic examples of Islamic financial corporations, the type of Islamic financial services that are provided, and the proposed methods to calculate the output of these Islamic financial services.

III. Consultation on the two unresolved issues[2]

10. **To resolve the first issue on the classification of the property income for those Islamic financial instruments which are classified as deposits, loans and debt securities,** it was proposed to consider terms such as "interest and similar investment returns" or "financing and investment income" to describe these returns. This was on the basis that while the returns on Islamic loans, deposits and debt securities have a parallel treatment to interest, these returns have a broader concept than interest.

11. **To assess the impact of the second issue, three economies, Indonesia, Malaysia and the State of Palestine, were invited to participate in empirical tests** to use a single reference rate to calculate the nominal FISIM on Islamic and conventional loans and deposits for each type of currency and separate reference rates to calculate the nominal FISIM on Islamic loans and deposits and FISIM on conventional loans and deposits. The results were quite different and implied the need for such tests to be conducted by more economies. Further, the empirical tests did not assess the impact on external trade in FISIM arising from using single and separate reference rates as only the estimates of total nominal FISIM were calculated.

12. **In November 2019, the TF and AEG were subsequently consulted on the following:**
    a. Is there a need to consider the interpretation that while the returns on Islamic loans, deposits and debt securities have a parallel treatment to interest flows, these returns have a broader concept than interest? If yes, can terms such as "interest and similar investment returns" or "financing and investment income" be used to describe these returns? If yes, which term would be preferable?

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[1] The IMF's 2019 Financial Soundness Indicators (FSI) Compilation Guide contains the classification of the Islamic financial instruments reported in the MFSMCG and provides guidance on how to map the financial information from the income statement, balance sheet, and other related information of Islamic deposit takers to the FSI's financial statements for deposit takers. For more information, see https://www.imf.org/en/Data/Statistics/FSI-guide.

[2] For more information on the two issues including the proposed solutions and results of the empirical tests, see the paper on Islamic finance in the national accounts on https://unstats.un.org/unsd/nationalaccount/aeg/2019/M13_5_4_Islamic_Finance.pdf.

b. Does the TF/AEG agree that further work is needed to assess the use of single versus separate reference rates in the calculation of FISIM in economies with conventional and Islamic finance?

13. **Most of the respondents agreed that while the returns on Islamic loans, deposits and debt securities have a parallel treatment to interest flows, these returns have a broader concept than interest.** However, they appeared split on the appropriate term to describe these returns. Slightly over half agreed that the term "financing and investment income" should be used over "interest and similar investment returns". Of those who disagreed with using the term "financing and investment income", one noted that this term is already being used by the Islamic Financial Services Board to describe the investment income flows for Islamic financial instruments that cover more than Islamic loans, deposits and debt securities. Mainly for this reason, he preferred the term "interest and similar investment returns" or "interest and similar Islamic finance investment returns". The same respondent also noted the need for more co-ordination between international and regional organizations working on this topic.

14. **A majority of the respondents also agreed that further work is needed to assess the use of single versus separate reference rates in the calculation of FISIM in economies with conventional and Islamic finance,** due to the fact that the results of the empirical tests showed that the differences in nominal FISIM when using a single reference rate and separate reference rates in the case of Indonesia and the State of Palestine appeared to be quite significant. Of those who disagreed, one doubted that further work will give additional insights. Another felt the decision to use single or separate reference rates should be left to the compiling agency, while a third recommended that the SNA guidance should be followed.

IV. Overview of work program of the joint task team

15. **The IFTT will undertake further work and finalize consistent recommendations from the perspective of national accounts and external sector statistics for the following issues:**

a. Classification of Islamic financial instruments and their corresponding property income.
b. Sectorization of Islamic financial corporations and the methods to calculate their output.
c. Calculation of FISIM in economies which have Islamic and conventional finance.
d. Possible changes/additions in the current *2008 SNA* and *BPM6,* including terminology and definitions.

16. **The key output of the IFTT will be summarized in a guidance note which will be presented for endorsement at the AEG and BOPCOM meetings in 2021.** The guidance note will comprise a set of recommendations for the classification of Islamic financial instruments and their corresponding property income, the sectorization of Islamic financial corporations and the measurement of output of Islamic financial corporations in both the

national accounts and external sector statistics, as well as possible revisions/additions to the *2008 SNA* and *BPM6*. Where appropriate, these recommendations should take into account the impact on the international comparability of macroeconomic aggregates such as debt and money supply.

17. **The guidance note will also recommend how the national accounts and external sector statistics can be nuanced to accommodate Islamic transactions, flows and positions,** including the classification of the property income for those Islamic financial instruments which are classified as loans, deposits and debt securities. Further, it will provide guidance on what reference rate(s) to use in the calculation of FISIM (including in external sector statistics) in economies which have conventional and Islamic financial activities, after assessing the results of more empirical tests. The starting point for the development of these recommendations will be the recommendations which have already been developed in the context of the national accounts by the TF as well as the comments by the AEG and TF during the consultation in 2019. Where appropriate, these recommendations and the accompanying matrices and diagrams in annexes 3 to 5 will be refined or expanded to provide consistent guidance on the statistical treatment of Islamic finance in the national accounts and external sector statistics, including the functional categories of investments; the sectorization of Islamic banks with multiple activities and Islamic windows; economic ownership of non-financial assets related to sales, lease, and equity financing which are legally owned by Islamic financial corporations; and transactions, other flows and positions in Islamic insurance (takaful and re-takaful). Annex 6 provides an overview of the issues to be addressed for each research topic, which were agreed by the IFTT at its inaugural meeting on 10 September 2020. In addition, annex 7 provides an overview of the tentative timeline for the preparation of the guidance note.

Annex 1: Intersecretariat Working Group on National Accounts/Balance of Payments Committee Joint Task Team on Islamic Finance
Terms of Reference

Introduction

1. Islamic finance does not operate in the same way as conventional banking as it follows the Shari'ah Islamic law, principles and rules. The Shari'ah Islamic law does not permit receipt and payment of "riba" (interest), "gharar" (excessive uncertainty), "maysir" (gambling), and short sales or financing activities that it considers harmful to society. Instead, the parties must share the risks and rewards of a business transaction and the transaction should have a real economic purpose without undue speculation, and not involve any exploitation of either party.

2. The Islamic financial standard setting bodies, such as the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB), have developed Islamic finance standards, including standards on accounting, auditing, governance, regulatory framework, capital adequacy, and risk management framework.[3] These efforts are aimed at harmonizing practices and principles of operation and recording within the Islamic financial system and ensuring effective integration into the international financial system.

3. The international statistical standards, however, do not sufficiently cover the integration of Islamic finance into macroeconomic and financial statistics. The only reference and brief guidance is provided in Annex 4.3 of the International Monetary Fund's (IMF) *Monetary and Financial Statistics Manual and Compilation Guide* (*MFSMCG*), which provides a detailed description of how Islamic financial corporations (IFIs) operate under the Islamic principles and how the instruments they use differ from conventional financial instruments. The *MFSMCG* describes the principal characteristics of Islamic financial assets and liabilities, and their classification by type of conventional financial instrument within the framework of monetary and financial statistics in line with the *System of National Accounts* 2008 (2008 SNA).

4. There is a need for further integration of Islamic finance and related principles/concepts into macroeconomic and financial statistics, necessitating the development of additional methodological and practical guidance. In the context of the implementation of the *2008 SNA* recommendations for Islamic finance as well as the need for guidance on the statistical treatment of Islamic instruments and income, questions were raised during several meetings in the Arab Region organized by the United Nations Economic and Social Commission for Western Asia (ESCWA). More recently, the issue of statistical treatment of Islamic finance has gained also attention as the international statistical community agreed to launch an update of international statistical standards at the 51st session of the United Nations Statistical Commission in March 2020.

[3] For example, the Executive Board of the International Monetary Fund (IMF) endorsed in May 2018 the use of the Core Principles for Islamic Finance Regulation (CPIFR) developed by the IFSB with the participation of the Secretariat of the Basel Committee on Banking Supervision, which provide a set of core principles for the regulation and supervision of the Islamic banking industry and are designed to take into consideration the specificities of Islamic banks.

5. Different positions emerged during these meetings/discussions. They can be summarized and grouped into the following two broad approaches:

- **Position 1:** The principles/concepts of Islamic finance, Islamic financial instruments and their corresponding property income, and Islamic financial corporations and their output can be fully integrated and bridged into the conventional statistical frameworks, without necessarily a need to revisit those frameworks.

- **Position 2:** The full integration and proper capturing of principles/concepts of Islamic finance, Islamic financial instruments and their property income, and Islamic financial corporations and their output warrant additional methodological articulations and perhaps consideration of new or hybrid types of financial instruments and property income and additional instrument and/or sector breakdowns. This is because certain Islamic financial instruments and financial corporations have different features as compared to those defined in the current statistical standards. Therefore, the creation of additional instruments and/or categories in the income and financial accounts or disaggregation between Islamic and conventional finance may be required to fully reflect the unique features of Islamic finance.

6. The issue of Islamic Banking was discussed by the Advisory Expert Group (AEG) on National Accounts at its 10th meeting in Paris, France, in 2016.[4] The AEG noted the difference in business arrangements between Islamic banking and conventional banking and recognized the systemic importance of Islamic banking for some economies and their relative rapid growth. The AEG agreed that further research on the statistical implications of Islamic banking in the national accounts is required and that practical guidance on the treatment of Islamic finance needs to be developed. As a result, an ISWGNA task force was formed to conduct further research on the statistical implications of Islamic finance in the national accounts and develop practical guidance on the treatment of Islamic finance transactions. Besides electronic consultations and meetings, the task force also organized two face-to-face meetings in 2017 and 2018 to discuss the progress of the work and draft recommendations and guidance.[5]

7. During the 2019 meeting of the IMF Balance of Payments Committee (BOPCOM), it was agreed that there is a need for guidance on the statistical treatment of Islamic finance in macroeconomic statistics in general and in external sector statistics (ESS) in particular. BOPCOM agreed to establish a dedicated taskforce to develop the necessary guidance for its consideration.

8. Given the existence of the Task Force on Islamic finance under the Inter Secretariat Working Group on National Accounts (ISWGNA) and the need for consistent guidance across different macroeconomic datasets, the ISWGNA and BOPCOM agreed to join forces in the same task team that includes both members selected by the ISWGNA and by BOPCOM. This joint task team, which is part of the international initiative to update the2008 SNA/BPM6, will prepare a

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[4] For more information, see http://unstats.un.org/unsd/nationalaccount/aeg/2016/M10.asp.
[5] For more information, see https://unstats.un.org/unsd/nationalaccount/RAmeetings/TFOct2017/lod.asp and https://unstats.un.org/unsd/nationalaccount/rameetings/tfoct2018/lod.asp.

joint guidance note on the treatment of Islamic finance in national accounts and in ESS, building on the work carried out by the task force in the past couple of years, detailing its research activities and explaining the recommendations for consideration by both the ISWGNA/AEG and BOPCOM.

Objectives

9. The joint task team on Islamic finance has been established by the ISWGNA and BOPCOM to carry out further research and develop methodology/guidance on the treatment of Islamic finance in national accounts and ESS.

10. The specific objectives of the joint task team are the following:

- Review the current practices, structure, classification of Islamic financial instruments and their property income;
- Assess whether changes in the methodology of national accounts and ESS are required to allow for full and proper reflection of Islamic finance in macroeconomic and financial statistics;
- Assess whether or not the Islamic Banks should be considered in the same way as conventional banks, or as managers of mutual funds or non-money market funds;
- Assess the statistical implications of either choice above; and
- Based on the outcomes of the above assessments, provide detailed guidance on the classification and recording of the Islamic financial instruments and their property income, Islamic financial transactions, and Islamic financial corporations and their output in the national accounts and ESS.

Governance and participation

11. The joint task team is established by the ISWGNA and BOPCOM and is chaired by Amina Khasib (State of Palestine) and Mounir Rhandi (Morocco). The Secretariat will be provided by UNSD and ESCWA.

12. The membership of the joint task team should include experts in the areas of national accounts, ESS, and other macroeconomic statistics from countries where Islamic finance is prevalent, and experts from relevant international/regional organizations. It is expected that members of the joint task team will actively engage in the discussions and the drafting of the guidance note and recommendations for discussion.

13. The working arrangements are expected to consist mainly of electronic communication through the circulation of documentation and the collection of comments on specific topics. Face-to-face meetings of the joint task team could be organized if necessary.

Reporting

14. The joint task team will report to the ISWGNA and BOPCOM in accordance with the SNA update procedures as established by the United Nations Statistical Commission[6] and the balance of payments update procedures established by the IMF[7], respectively.

Overall coordination

15. To ensure overall consistency on cross-cutting issues and no duplication of work, UNSD (representing the SNA community) and BOPCOM's Balance of Payments Task Team are responsible for the overall coordination between the task teams and their work streams. The aim is to facilitate the exchange of information between the task teams and to align the work plans as appropriate.

Timeline

16. The work will take place during April 2020 – September 2021. The following key deliverables and timetable are currently envisaged:

a. Joint information note (ISWGNA/BOPCOM) submitted to the next AEG and BOPCOM meetings in 2020.
b. Final joint guidance note (ISWGNA /BOPCOM) to be presented at the 2021 AEG and BOPCOM meetings.

[6] See http://unstats.un.org/unsd/nationalaccount/uProc.asp.
[7] See https://www.imf.org/en/Data/Statistics/BPM.

Annex 2: Intersecretariat Working Group on National Accounts/Committee on Balance of Payments Statistics Joint Task Team on Islamic Finance

Members

No.	Name	Economy/Organization
1	Mr. Mounir Rhandi (co-chair)	Morocco
2	Ms. Amina Khasib (co-chair)	State of Palestine
3	Ms. Wafa Aboul Hosn (secretariat)	ESCWA Statistics Division
4	Mr. Omar Hakouz (secretariat)	ESCWA Statistics Division
5	Mr. Herman Smith (secretariat)	UNSD
6	Mr. Benson Sim (secretariat)	UNSD
7	Mr. Suswandi	Indonesia
8	Mr. Mohd Yazid Kasim	Malaysia
9	Ms. Norhayati Razi	Malaysia
10	Ms. Bouchra Farghsaoui	Morocco
11	Ms. Derya BAŞ Sonbul	Turkey
12	Mr. Abd El Shafi El Ashmawy	United Arab Emirates
13	Mr. Perry Francis	United Kingdom
14	Mr. Omar Mustafa Ansari	AAOIFI
15	Mr. Mohammad Majd Bakir	AAOIFI
16	Mr. Rizwan Malik	AAOIFI
17	Mr. Alick Mjuma Nyasulu	ESCAP
18	Mr. Ahmed Al Farid	GCC-Stat
19	Dr. Abideen Adeyemi Adewale *	IFSB*
20	Dr. Aminath Amany *	IFSB*
21	Ms. Samah Torchani	IMF
22	Mr. Levan Gogoberishvili	IMF
23	Mr. Artak Harutyunyan	IMF
24	Mr. Malik Bani Hani	IMF
25	Mr. Ousmane Seck	IsDB
26	Mr. Rodolfo Ostolaza	OECD
27	Dr. Atilla Karaman	SESRIC
28	Mr. Abdulhamit Ozturk	SESRIC

No.	Name	Economy/Organization
29	Mr. Ragheed I. Moghrabi	RH University
30	Dr. Tawfik Azrak	Social Sciences University of Ankara
31	Mr. Russell Krueger	Independent consultant

* - Observer

Alternates

No.	Name	Economy/Organization
1	Ms. Hana Dwi Kristanti	Indonesia
2	Ms. Nurul Ainun Nisa	Indonesia
3	Ms. Khairul Aidah Samah	Malaysia
4	Mr. Mohd Fahmi Mohd Arupin	Malaysia
5	Siti Sarah Che Dan	Malaysia
6	Ms. Jihane Bennani	Morocco
7	Ms. Husniye Aydin	Turkey
8	Mr. Michael Lyon	United Kingdom

Annex 3: Classification of Islamic financial instruments and corresponding property income

A- Sources of funds

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
1	Qard, Wadiah, Amanah	Deposits that can be withdrawn, at par, without penalty or restriction, and are generally usable for making payments by check, draft, giro, or other direct payment facilities. Are not linked to any profit-making ventures and are not part of profit and loss sharing schemes.	Transferable deposits (F22) if they are directly usable for making payments by check, draft, giro order, direct debit, or direct payment facility. Otherwise, classified as Other deposits (F29)	Usually offer no or very small returns to depositors on the basis of gift (hibah) which cannot be stipulated in the contract.	Interest (D41)
2	Mudaraba (also known as profit-sharing investment account)	A contract between investors and an Islamic financial institution (IFI) that, as a silent partner, invests the deposits in a commercial venture. Also, Interbank Mudarabah between banks/financial institutions is a wholesale money market transaction designed as liquidity management instruments in the Islamic Money Market. Profit sharing of the venture is pre-determined on the basis of risk and return, and the IFI and investors share any profit generated from the venture. A Mudaraba can	(2a) Restricted Mudaraba – Other deposits (F29) (2b) Unrestricted Mudaraba i. Unrestricted Mudaraba without fixed period – Other deposits (F29) ii. Unrestricted Mudaraba accepted for a fixed period but not negotiable – Other deposits (F29)	Share of profit	Interest (D41) if classified as deposits or debt securities Dividends (D421) if classified as equity

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
		be entered into for a single investment or on a continuing basis with the IFI acting as a fiduciary. There are two types of Mudaraba investment accounts according to the AAOIFI FAS No. 27 (Investment Accounts), namely Restricted Mudaraba (2a) and Unrestricted Mudaraba (2b). **(2a) Restricted Mudaraba** is where the investor restricts the manner as to where, how, and for what purpose the funds are invested. No mixing of funds is allowed from other sources to ensure proper management and accountability of the funds. A separate disclosure (off-balance sheet) in the form of Statement of Restricted Mudaraba is required to be kept by the IFIs. **(2b) Unrestricted Mudaraba** is where the investor fully authorizes an IFI to invest the funds without	iii. Unrestricted Mudaraba accepted for fixed period and arranged through negotiable instruments – Debt securities (F3) unless it provides a claim on the residual value of the issuing entity, in which case it is classified as Equity (F51)		

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
		restrictions as to where, how, and for what purpose the funds should be invested as long as it is deemed appropriate. Mixing of funds from other sources (including shareholders' funds) is permitted and separate disclosure in the financial statement is therefore required. Similar to the case of deposits at conventional financial institutions, Unrestricted Mudaraba can be divided into the following types: i. Mudaraba accepted without a fixed period. The investors are free to withdraw their money at any time. ii. Mudaraba accepted for a fixed period that provides an opportunity for IFIs to invest in more profitable long-term projects. This type of Unrestricted Mudaraba is similar to time deposits at conventional financial institutions and usually			

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
		generates higher profits in comparison to the former type. iii. Mudaraba accepted for fixed periods and arranged through negotiable instruments (called investment deposit certificates or Mudaraba Certificates). This type of Unrestricted Mudaraba has characteristics similar to those of debt securities unless it provides a claim on the residual value of the issuing entity, in which case it is classified as equity.			
3	Qard-Hasan	Return-free deposits voluntarily placed by depositors, to participate in the financing for needy individuals or for social purposes. Qard Hassan may also be provided by a depositor in specific situations. In all cases, it is interest-free and is meant to help stabilize cash flows or cater to financing needs that cannot be met using commercial arrangements.	Other deposits (F29)	No return	Interest (D41)

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
4	Participation term certificates	Long-term investment instruments that entitle the holder to a share of a corporation's profit.	Other deposits (F29) if certificate treated as debt liabilities Equity (F51) if part of the capital base	Share of profit	Interest (D41) if classified as debt liabilities Dividends (D421) if classified as equity
5	Profit and loss sharing certificates	Investors' deposits that somewhat resemble shares in a company but do not provide a claim on the residual value of the IFI and participation in its governance.	Other deposits (F29) if it is not negotiable Debt securities (F3) if it is negotiable	Share of profit	Interest (D41) if classified as other deposit Interest (D41) if classified as debt securities
6	Sukūk	Sukuk come in the following main types: 6(a) Debt-type Sukuk (where the underlying financing is by way of credit sales like Murabaha or Salam). 6(b) Equity-type Sukuk (where underlying financing is by way of profit-sharing ventures, assets, etc.).	Debt securities (F3) unless it provides a claim on the residual value of the issuing entity, in which case it is classified as Equity (F51)	Share of revenue	Interest (D41) if classified as debt securities Dividends (D421) if classified as equity

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Proposed classification of property income in 2008 SNA
		Generally, Sukuk are investment certificates issued by IFIs as a way to obtain funding. According to the IFSB-15 (Revised Capital Adequacy Standard for Institutions Offering Islamic Financial Services), Sukūk (plural of sakk) are certificates, with each sakk representing a proportional undivided ownership right in tangible and intangible assets, monetary assets, usufruct, services, debts or a pool of predominantly tangible assets, or a business venture (such as Mudaraba or Musharaka). Sukuk can be credit rated by rating agencies and listed on equity exchanges.			

Annex 3: Classification of Islamic financial instruments and corresponding property income

B- Uses of funds

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Classification of property income
1	Qard-Hasan financing	Return-free financing that is made to needy individuals or for some social purpose and the debtors are required only to repay the principal amount of the financing.	Loans (F4)	No return	Interest (D41)
2	Murabaha financing	A type of financing provided by an IFI to its client by supplying desired goods or services at cost plus an agreed profit margin with deferred payments. In a Murabaha contract, an IFI purchases goods upon the request of a client, who makes deferred payments that cover costs and an agreed-upon profit margin for the IFI. The IFI handles payments to the supplier including direct expenses incurred (delivery, insurance, storage, fees for letter of credit, etc.). Operating expenses of the IFI are not included. Under Murabaha contracts, disclosure of cost of the underlying goods is necessary.	Loans (F4)	Profit margin	Interest (D41)

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Classification of property income
3	Bai Muajjal	A type of financing provided by an IFI to its client by supplying desired goods or services with deferred payments. The difference with Murabaha is that the initial cost of the goods or service does not need to be disclosed by the IFI and settlement is based on credit (versus cash in Murabaha contracts). The price fixed for the commodity in a Bai Muajjal transaction can be the same as the spot price or higher or lower than the spot price.	Loans (F4)	Profit from higher good/service price	Interest (D41)
4	Bai Salam	A short-term agreement in which an IFI makes full prepayments (spot payment) for future (deferred) delivery of a specified quantity of goods on a specified date. Bai Salam is typically used to provide short-term financing of agricultural products.	Loans (F4)	Profit from a higher price for the goods	Interest (D41)
5	Istisna'a	A partnership between an IFI and an enterprise, usually manufacturer or construction company, in which the IFI places an order and provides	Loans (F4) if the produced goods/building are not for IFI's own use	Profit from a higher price for the goods	Interest (D41)

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Classification of property income
		financing to the enterprise to manufacture/construct and or supply certain goods or buildings.	Other account receivable (F8) if goods or building are for IFI's own use		
6	Ijarah	A lease-purchase contract in which an IFI purchases capital equipment or property and leases it to an enterprise. The IFI may either rent the equipment or receive a share of the profits earned through its use. Under Operating Ijarah the title for the underlying asset is not transferred to the client (lessee). A financing Ijarah involves two contracts (i.e., a lease over the lease period and transfer of ownership at the end of the contract).	Operating Ijarah – operating lease Financing Ijarah – Loans (F4)	Benefit from using the assets in productive activity Share of profit earned through using assets	Interest (D41)
7	Musharaka	A partnership between an IFI and an enterprise in which both parties (*arbab al maal*) contribute to the capital of partnership.	Loans (F4) unless the IFI acquires a claim on the residual value of the enterprise, in which case it is classified as Equity (F51)	Share of profit	Interest (D41) if classified as loans Dividends (D421) if classified as equity
8	Mudaraba financing	A partnership between an IFI and a client in which the IFI (*rab al maal*) provides capital and the client provides skillful labor whereby skill and money are brought together to	Loans (F4) Although Mudaraba financing has features of equity, it has a fixed-term claim on the client	Share of profit	Interest (D41)

No	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Classification of property income
		conduct business. Profits generated from the business are shared according to the agreement, while losses are borne fully by the IFI as the capital provider, except when losses were due to misconduct, negligence or violation of the agreed conditions by the client.	rather than a claim on any residual value.		
9	Tawarruq	A type of financing provided by an IFI with the intent to supply cash to its client. Tawarruq contracts are comprised of two parts: 1) A Murabaha contract where the client purchases a product from the IFI for a marked-up price on a deferred payment basis. 2) The client sells the good to a third party on a spot payment basis. In practice the IFI sells the good to the third party on behalf of the customer. This results in the client receiving cash on the spot with the obligation to pay the initial marked-up price of the good either in installments or as a deferred lump sum payment to the IFI.	Loans (F4)	Profit margin	Interest (D41)

Takaful

NO	Type of Islamic financial instrument	Description	Classification according to annex 4.3 of MFSMCG	Type of return payable to asset holder	Classification of property income
1	Takaful	An agreement between persons exposed to specific risks in order to avoid damages through creating a fund in which contributions are deposited on a voluntary basis. Participants receive compensation for damages from the occurrence of the insured risk.	Insurance, pension and standardized guarantee schemes (F6)	Investment income	Investment income attributable to insurance policy holders (D441)

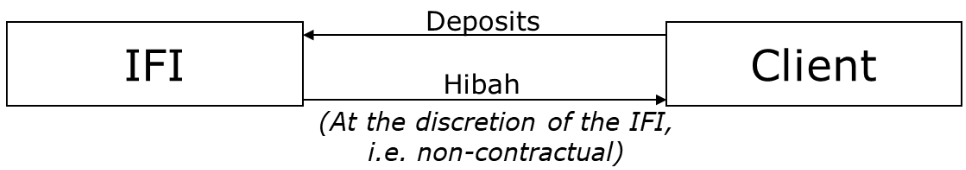
Notes

1. Interest (D41) on deposits and loans refers to SNA interest in the allocation of primary account and actual interest in the financial account.

Annex 4: Diagrams illustrating the flows between Islamic financial corporations and their clients for various Islamic financial instruments

A. Sources of Funds

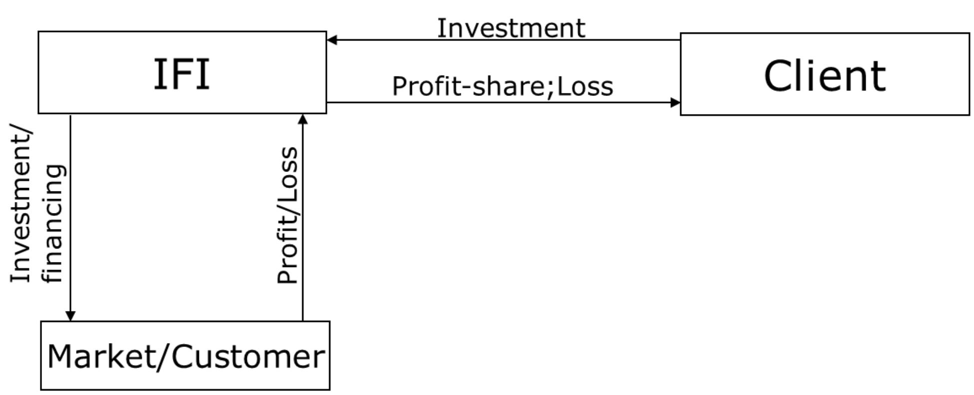
1) Qard, Wadiah, Amanah



- Transferable deposits (F22) if they are directly usable for making payments by check, draft, giro order, direct debit, or direct payment facility. Otherwise, classified as Other deposits (F29)
- Property income: Interest (D41)

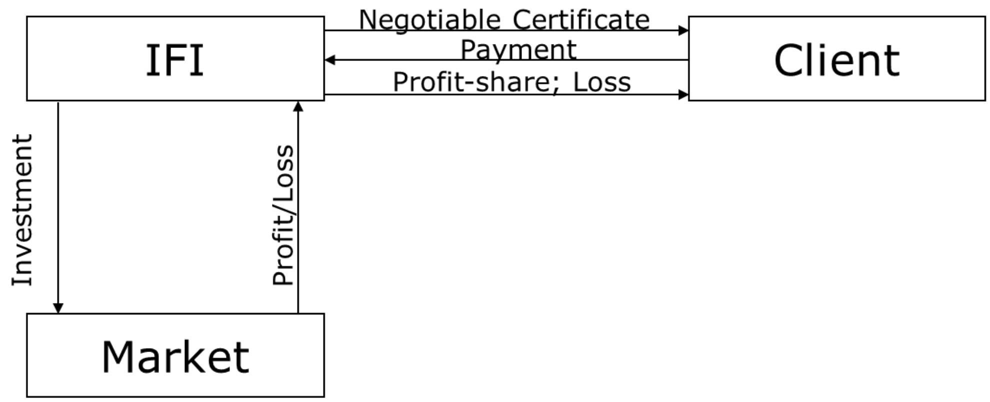
2a) Restricted Mudaraba

2bi) Unrestricted Mudaraba without fixed period
2bii) Unrestricted Mudaraba with fixed period but not negotiable



- Other deposit (F29)
- Property income: Interest (D41)

2biii) Unrestricted Mudaraba with fixed period and negotiable



- Debt securities (F3) unless the certificate provides a claim on the residual value of the issuing entity, in which case it is classified as Equity (F51)
- Property income: Dividends (D421) if classified as equity; Interest (D41) if classified as debt securities

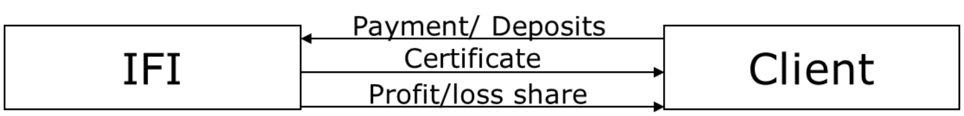
3) Qard-Hasan

- No actual return but there may be SNA interest
- Other deposits (F29)
- Property income: Interest (D41)

4) Participation term certificates

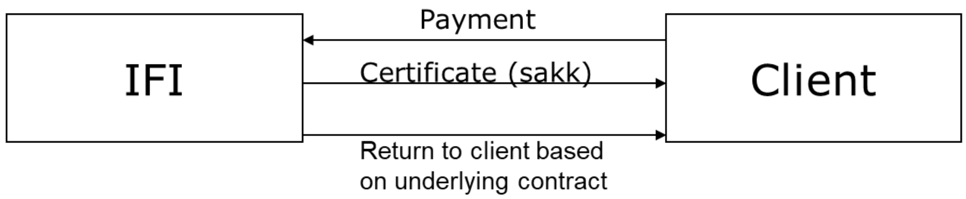
- Other deposits (F29) if certificate is treated as debt liability and issued by IFIs
- Equity (F51) if part of the capital base of non-financial enterprises
- Property income: Interest (D41) if classified as other deposits; Dividends (D421) if classified as equity

5) Profit and loss sharing certificates



- Other deposits (F29) if not negotiable
- Debt Securities (F3) if negotiable
- Property income: Interest (D41)

6) Sukuk

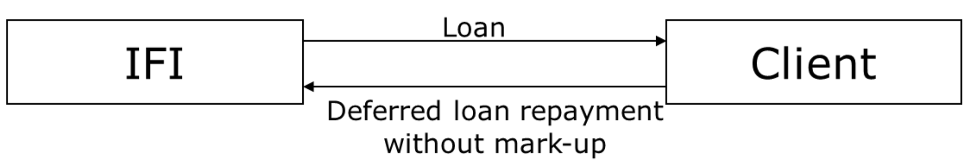


- Debt securities (F3) unless the owner of the security has a claim on the residual value of the issuing entity, in which case it is classified as Equity (F51)
- Property income: Interest (D41) if classified as debt securities; Dividends (D421) if classified as equity.

Annex 4: Diagrams illustrating the flows between Islamic financial corporations and their clients for various Islamic financial instruments –

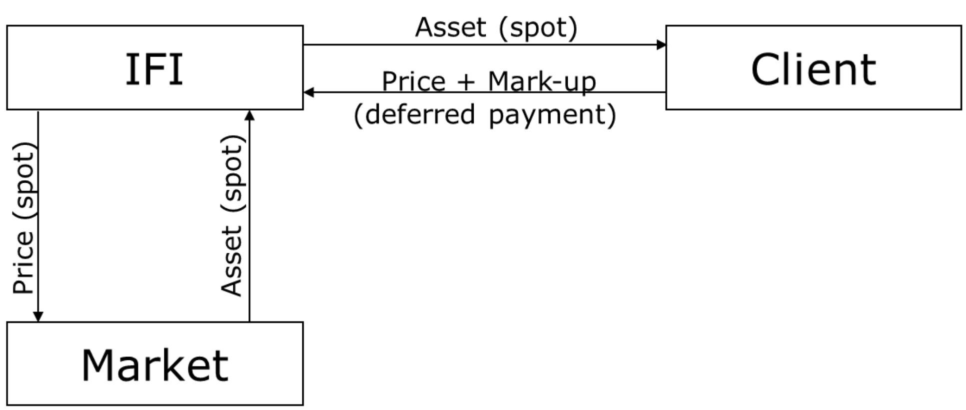
B. Uses of Funds

1) Qard-Hasan financing



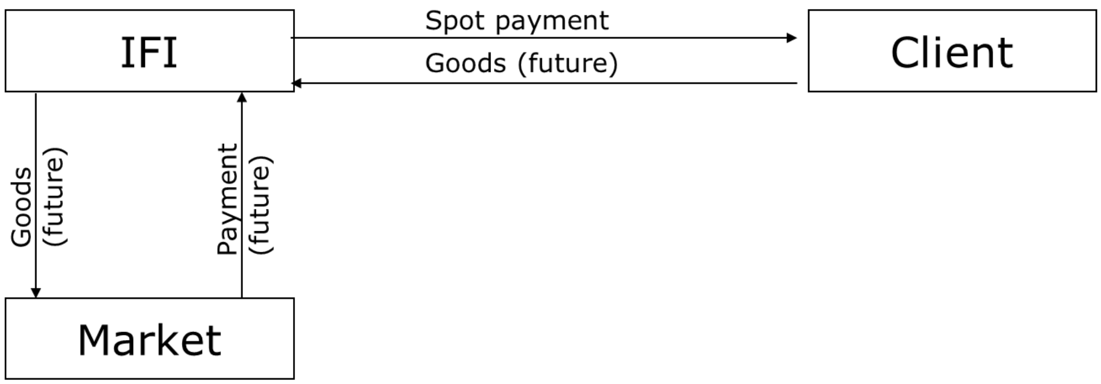
- Return-free financing for needy individuals or for some social purpose
- Loans (F4)
- Property income: No income generated from this financing

2) & 3) Murabaha/ Bai Muajjal



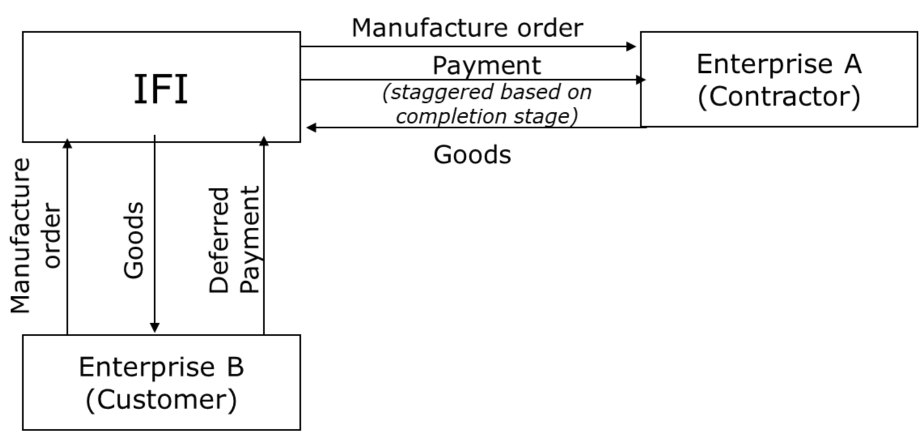
- In Bai Muajjal the initial price does not need to be disclosed to the client
- Loans (F4)
- Property income: Interest (D41)
- Question to consider:
  Who is the economic owner of the asset at which point in time?

4) Bai Salam



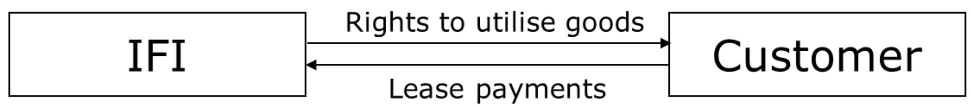
- The return is the difference between the spot payment and the actual value of the goods in the future
- IFI generally pays less (spot) than the future/actual value of goods
- Typically used to provide short-term financing of agricultural products
- Loans (F4)
- Property income: Interest (D41)

5) Istisna’a



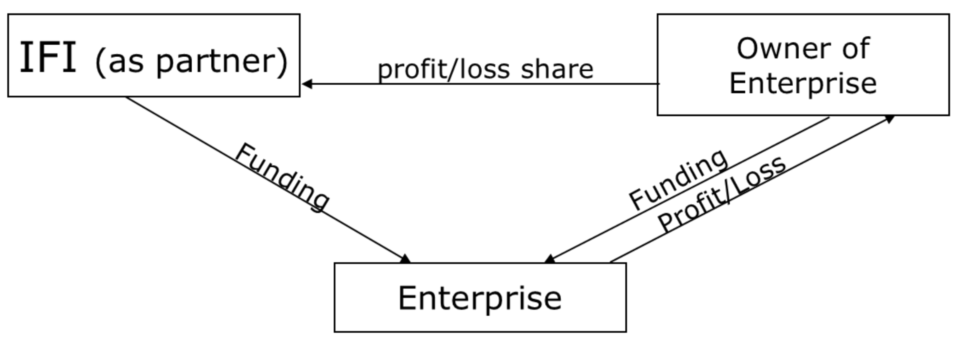
- The return is the difference between the payment to the Contractor and the deferred payment by the customer
- Typically used to finance construction and project financing
- Loans (F4) between IFI and Customer
- Other account receivable (F8) if goods or building are for IFI’s own use
- Property income: Interest (D41)

6) Ijarah



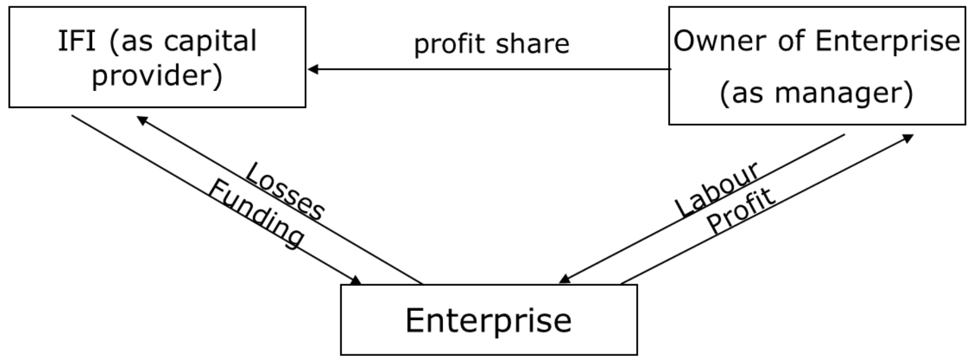
- Operating Ijarah – operating lease
- Financing Ijarah – Loans (F4)
- Property income: Interest (D41)
- Commonly used for hire purchase products

7) Musharakah



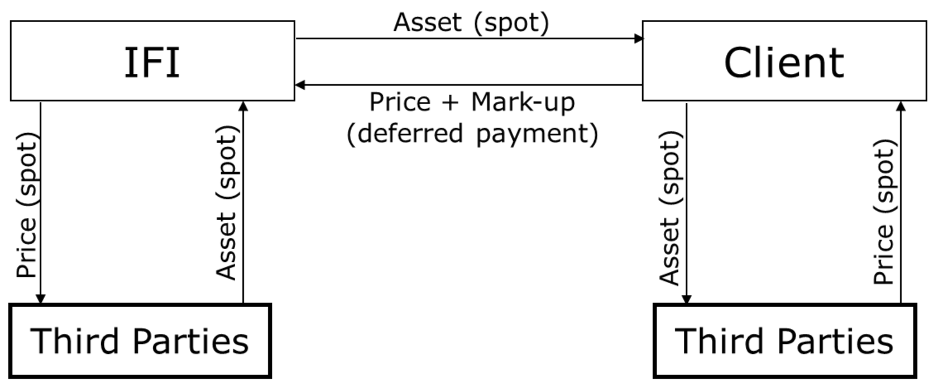
- Loans (F4) unless the IFI has a claim on the residual value of the enterprise then it is classified as Equity (F51)
- Property income: Interest (D41) if classified as loans; Dividends (D421) if classified as equity.

8) Mudaraba financing



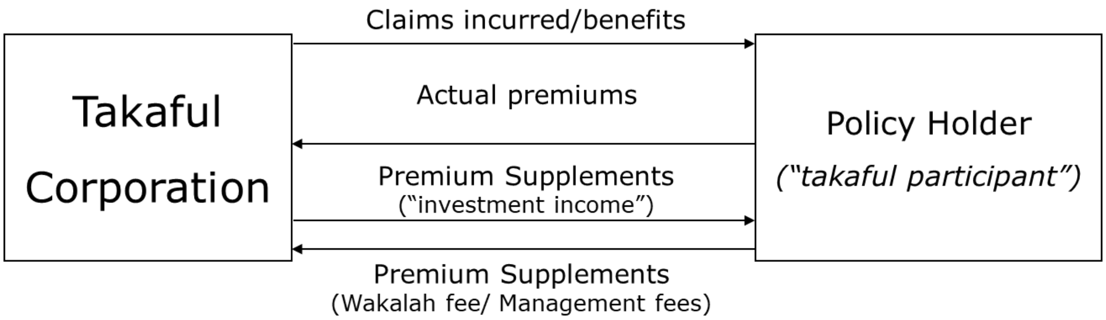
- Loans (F4)
- Property income: Interest (D41)

9) Tawarruq financing



- Loans (F4)
- Property income: Interest (D41)

10) Takaful



- Insurance, pension and standardized guarantee schemes (F6)
- Property income: Investment income attributable to insurance policy holders (D441)

Annex 5: Sectorization of Islamic financial corporations and methods to calculate output of Islamic financial corporations

Subsector	Generic examples	Examples of financial services provided	Proposed method to calculate output
Central Bank (S121)	Central Bank Monetary Authority	Monetary policy services Financial intermediation services Borderline cases, such as supervisory services	Sum of Cost FISIM formula Market output – explicit fees Non-market output – Sum of cost
Deposit-taking corporations except the central bank (S122)	Islamic Banks Commerce and Development Banks Online Banks Commercial Banks Islamic Microfinance Banks	Mudaraba Qard Tawarruq Murabaha Musharaka Ijarah Sharī`ah-compliant savings and current accounts	Output is a combination of the following: (a) For loans and deposits is calculated using the FISIM formula, i.e., $(r_L–rr)\times Y_L+(rr–r_D)\times Y_D$, where r_L, r_D, rr, Y_L and Y_D represent the loan dividend rate, deposit dividend rate, reference rate, average stock of loans and average stock of deposits respectively (b) Explicit fees
Money market funds (MMFs) (S123)	Sharī`ah-compliant MMFs	Sharī`ah-compliant investment services	For purposes of calculating the output, and thereby the value added, of Islamic MMFs, and based on the nature of ownership of shares, they could be treated in the same way as conventional MMFs. As such, output may be computed as the sum of various fees that MMFs charge investors on transactions, namely purchase and redemption fees, exchange fees, account fees, and operating fees. Retail fees (Bank –indididual investor) can differ from wholesale (Interbank market) fees.

Subsector	Generic examples	Examples of financial services provided	Proposed method to calculate output
Non-MMF investment funds (S124)	Sharī`ah-compliant Non-MMF investment funds	Sharī`ah-compliant investment services	For purposes of calculating the output, and thereby the value added, of Islamic non-MMFs, and based on the nature of ownership of shares, they could be treated in the same way as conventional non-MMFs. As such, output may be computed as the sum of various fees that non-MMFs charge investors on transactions, namely purchase and redemption fees, exchange fees, account fees, and operating fees.
Other financial intermediaries except insurance corporations and pension funds (S125)	Islamic investment banks Investment companies	Sharī`ah-compliant (advisory) investment banking services such as structured finance (Istisna'a or Ijarah), investment placement, raising funds (often on the basis of joint Mudaraba) in equity and debt markets and trade finance (Murabaha contracts being the dominant Sharī`ah principle) Murabaha or Bai Ajel installment sales	Output is a combination of the following: (a) Explicit fees (b) Implicit financial service charge, which is calculated as calculated as $(r_L – rr) \times Y_L$, where r_L , rr and Y_L represent the lending return, reference rate and average stock of loans respectively
Financial auxiliaries (S126)	Asset management corporations complying with Sharī`ah	Management of Sharī`ah-compliant investments and funds	Explicit fees Sum of Cost

Subsector	Generic examples	Examples of financial services provided	Proposed method to calculate output
	Islamic finance advisory boards	Brokerage (e.g. Takaful products) Provision of infrastructure for financial markets such as, financial software or capital market hubs In many countries Islamic Financial Institutions need to appoint a Sharī`ah advisor.	
Captive financial institutions and money lenders (S127)	Holding companies Sharī`ah-compliant money lenders	Holding of assets (i.e., controlling-levels of equity) of subsidiary corporations which provide Islamic financial services Sharī`ah-compliant money lending services	Output is calculated as the value of explicit fees or sum of costs Output is a combination of the following: (a) Explicit fees (b) Implicit financial service charge, which is calculated as calculated as $(r_L – rr) \times Y_L$, where r_L , rr and Y_L represent the lending return, reference rate and average stock of loans respectively
Insurance corporations (S128)	Takaful Re-Takaful	Life Takaful Non-life Takaful Re-Takaful	Nature of Takaful business does not differ much from conventional insurance except for profit/risk sharing. Proposed recommendation for calculating output: Life Takaful

Subsector	Generic examples	Examples of financial services provided	Proposed method to calculate output
			Output is calculated as actual premiums earned plus premium supplements minus benefits due minus increase (plus decrease) in actuarial reserves and reserves for with-profits insurance Non-life Takaful Output can be calculated using either one of the three following methods: (a) Output is calculated as actual premiums earned plus expected premium supplements minus expected claims incurred, where expected claims and premium supplements are estimated from past experience (expectations approach); (b) Output is calculated as actual premiums earned plus premium supplements minus adjusted claims incurred, where adjusted claims are determined by using claims due plus the changes in equalization provisions and, if necessary, changes to own funds (accounting approach); (c) Output is calculated as the sum of costs (i. e., intermediate consumption, compensation of employees, capital costs and other taxes (less subsidies) on production) plus an allowance for "normal profit". Re-Takaful Output is calculated as actual premiums earned less commissions payable plus premium supplements

Subsector	Generic examples	Examples of financial services provided	Proposed method to calculate output
			minus both adjusted claims incurred and profit sharing
Pension funds (S129)	Defined contribution pension funds Defined benefit pension funds	Pension fund services	Sum of costs

Annex 6: List of research topics

Research topic	Description	Overview of issues
A	Terminology for property income for Islamic loans, deposits and debt securities	Consider terms such as “interest and similar investment returns” or “financing and investment income” to reflect the broader concept of these returns. Nuance the SNA and BPM to reflect these returns.
B	Reference rates and terminology for calculating Islamic and conventional FISIM in the context of national accounts and external sector statistics	Reflect the terms recommended in (a) in calculation of FISIM. Clarify the reference rate(s) to use to calculate national and external trade for FISIM on Islamic and conventional loans and deposits which are denominated in the same currency. Assess whether to conduct empirical tests in more economies.
C	Statistical treatment of Islamic finance in external sector statistics and national accounts, including the functional categories of investments	Assess how the recommendations that have been developed by the ISWGNA task force on Islamic finance can be refined so that they can be applied in external sector statistics. Align the recommendations such as classification of Islamic financial instruments with functional categories of investments in external sector statistics.
D	Sectorization of Islamic banks with multiple activities and Islamic windows	Assess if Islamic banks with multiple activities should be classified in the deposit-taking corporations except the central bank subsector (S122). Assess if Islamic windows can be considered as institutional units. If yes, recommend the appropriate subsector of the financial corporations sector to classify these units. Recommend if the SNA and BPM should be refined or expanded to provide explicit criteria on classifying Islamic banks with multiple activities into S122 and Islamic windows.

Research topic	Description	Overview of issues
E	Economic ownership of non-financial assets related to sales, lease, and equity financing which are legally owned by Islamic financial corporations	Assess whether the economic owner of such non-financial assets should be the borrowing unit or the Islamic financial corporation who may be the legal owner only briefly. If the economic owner is the borrowing unit, assess at which point the change in economic ownership should be recorded.
F	Transactions, other flows and positions in Islamic insurance (takaful and re-takaful)	Align the specific business arrangements and terminologies with the concepts and terminologies in the national accounts and external sector statistics to facilitate the recording of Islamic insurance transactions as services, primary and secondary income as well as positions in the national accounts and external sector statistics.

Annex 7: Tentative timeline for preparation of guidance note

Activity	Date
First draft of the Sub-task teams guidance notes by authors	25-Dec-20
Review by Chairs and Secretariat	15-Jan-21
Consultations within IFTT	Jan-21
First draft of guidance note	Mar-21
Preliminary review by AEG/ISWGNA & BPTT	Apr-21
Wider public consultation	Jun-21
Finalization of guidance note	Aug-21
Presentation to AEG/ISWGNA and BOPCOM for endorsement	Oct-21
Testing of recommendations, if necessary	Jun-22