

Global Wealth Management: How does the Muslim world do it?

“Global Attitudes to Islamic Wealth Management” is an enlightening and unprecedented report compiled by Jersey Finance, a not-for-profit organisation representing Jersey as an international finance centre (IFC), in partnership with Gateway Global, a team of Shari’a experts, lawyers, financiers, accountants and regulators well versed in multi-jurisdictional legal practice. This report sheds light on the specifics of the Islamic legal framework for wealth management as well as the views and attitudes of Muslim high-net-worth and ultra-high-net-worth individuals (HNWIs/UHNWIs) and family offices towards key elements of wealth management i.e. succession planning, fiduciary planning, inheritance, tax, current and future demands for investment products, ethical alignments and the distinctions between different jurisdictions.

The importance of understanding Shari’a compliant wealth management is paramount as the potential of this particular sector of the financial services industry remains understated despite the Islamic finance industry totalling US\$2.8 trillion in assets¹. Although in the past 20 years international investment banks have made Shari’a compliant financial instruments increasingly sophisticated in structure, which have been in turn successfully distributed by private and/or retail banks, the level of innovation has decreased substantially preventing maximum market growth. This has restricted the versatility and supply of Islamic products and services despite substantial demand Islamic private wealth management services. Recent spikes of activity in the Islamic finance industry, however, suggest a rebounding interest in the supply side; intermediary companies, regulators and related stakeholders have begun working towards closing the product gap by tackling fundamental policy and infrastructural issues. The trend towards socially responsible investing (SRI) and environmental, social and governance (ESG) standards has become an important catalyst for the accessibility and visibility of Shari’a compliant management, especially “NextGen” individuals desiring social returns on their investments. HNWIs/UHNWIs were responsible for the international growth of the Islamic finance industry at the onset of the 21st century and for the new generation of socially conscious HNWIs/UHNWIs to further expand and elevate this finance market in the international arena it is pertinent for the Islamic wealth management industry to be acutely aware of the Muslim private wealth market’s views and needs to provide quality products and services.

Background on the Shari’a Framework for Islamic Wealth Management

To understand the complexities of the Islamic finance market it is necessary to be familiar with the terms and conditions instated by the Shari’a law on Muslims. According to Shari’a law, wealth and succession are civil acts that are governed by the Islamic jurisprudential framework of *fiqh al muamlat* (jurisprudence of transactions) which is based on the knowledge revealed to the Muslim world through the Holy Book *Qur’an* and the teachings and traditions of the Holy Prophet Muhammad (PBUH) [Peace be upon him] collectively called *Ahadith*. The framework is based on the principles of familial unit preservation (prevention of disputes based on wealth), equitable distribution, maintaining a robust social welfare system, and providing “reasonable”

¹ https://icd-ps.org/uploads/files/ICD-Refinitiv%20IFDI%20Report%2020201607502893_2100.pdf

leeway for personal decision making regarding one's wealth. In Islam, the quintessential doctrine is that "deeds are based on intentions" which is why spending and giving generously during one's lifetime is encouraged as a prime means for trade and for proper wealth circulation flows within the society to ensure equitable wealth for all. Equality is another crucial element within Shari'a; when a Muslim is to give wealth to an equal class of recipients, for example, one's children, it is obligatory for the value of the gift to be equal unless the giving is based on needs in which case the amount must be exactly the amount that is needed. Based on these principles, Shari'a law outlines specific protocols for wealth transfer as listed below:

- *Faraidh*; inheritance
- *Wassiya*; Property transfer to another as a bequest which does not infringe upon inheritance rights
- *Waqf*; Endowment of an asset for a charitable cause usually under a trust
- *Hiba*; voluntary gift
- *Luqata*; lost property that is found and safely kept for a minimum of three weeks before it becomes permissible for the finder to keep it as their own
- *Umra'ruqa*; property bestowed to another during donor's lifetime to be transferred upon donor's death
- *Zak'ah*- Obligatory annual wealth tax of 2.5% on all Muslims

Muslims are allowed a great deal of agency over their wealth during their lifetime provided they remain within the boundaries of the broad parameters listed previously; however, upon the death of a Muslim, Islam imposes strict terms and conditions for inheritors and their shares in explicit detail to prevent any familial disputes. It is not unheard of for some stakeholders to attempt to bypass certain parameters via legal gambits that may seem Shari'a compliant on the surface level due to which Islamic scholars strictly advise against non-Islamic arbitration.

Rules for the Islamic Wealth Succession Framework

Unlike the rule of primogeniture whereby the firstborn has the sole right of succession, the Islamic framework for succession stipulates equitable distribution for all family members one may feel obligated to provide for within the fixed quotas stipulated by the *fiqh al muamlat*. According to the *Qur'an (4:11)*, and *(4:12)* succession ratios are as follows:

For male deceased:

- Male relatives to receive twice the portion of female relatives (1 son 1 daughter: $\frac{2}{3}$ and $\frac{1}{3}$ respectively)
- If only two or more daughters: $\frac{2}{3}$ of the total inheritance
- If only one daughter: half of total inheritance
- For parents of deceased with children: $\frac{1}{6}$ to each
- For parents of deceased with siblings: only mother given $\frac{1}{6}$
- For parents of deceased with no children or siblings: mother inherits $\frac{1}{3}$

For female deceased

- If the deceased has no children then the spouse receives $\frac{1}{2}$ of the total inheritance
- If the deceased has children, the spouse receives a quarter whilst the children inherit the remaining (in accordance with the 1:2 principle between male and female children mentioned above)

Shares of inheritance are directly proportional to the level of closeness of relatives and their respective financial burdens and as such, each beneficiary's share can be accurately calculated based on the number of relatives surviving the deceased. As a general rule, only the parents, spouses, and children are entitled to primary shares however progressively distant relativism such as uncles, grandparents, cousins etc., can be given due shares if the deceased does not have any of the first class of relatives. The deceased's siblings will only inherit a share of the inheritance if the deceased has neither parents nor children survive them. Overall, shares in inheritance are calculated as fixed fractions of estates and other assets rather than being divided as whole estates or assets per beneficiary. The only time an heir may be denied their inheritance is in the case of them forsaking Islam as their religion or being involved in the murder of the deceased.

The reason for male successors receiving larger shares than their female counterparts is due to the responsibility put on male successors to financially support other members of the family whereas female successors are not promulgated to spend beyond general charity; whatever they wish to give to relatives is considered altruistic giving. When such financial requirement is not imposed then male and female relatives (of the same degree of closeness) inherit equal shares. A Muslim may also wish to leave portions of their wealth for more needy relatives, acquaintances, charities or whosoever provided these portions do not exceed more than $\frac{1}{3}$ of their total wealth as *wassiyah*, and Shari'a ensures that such allowance is only given off once sufficient wealth for the deceased's dependants has been distributed successfully. In regards to the rights of the spouse, their share of inheritance is comparatively smaller against the majority share they may be entitled to under Western norms but under Shari'a law, there is an additional responsibility thus put on the closest male relative (usually the son shared between the deceased and their spouse) to look after the spouse's needs and financial security. For wives, in particular, the *Qur'an* has ordained a sizable but specific portion as well as shelter and a minimum of one year's worth of maintenance for the wife and her dependants.

The English Legal Framework and Rules for Wealth Management

It is quite interesting to note that Shari'a law and English law are quite compatible, with English law being amongst the most preferred choice of law for Muslims for contracts and financing structures. In OECD countries and IFCs like Jersey, English law also presents itself as a solid standard for inheritance and succession. The report explains that Jersey's law is a highly sophisticated legal system with several similar points with English law. High net worth families therefore often set up their holding companies in such jurisdictions as they can simultaneously benefit from English law as the governing law to gain contracts related to positive revenue from

investments in other jurisdictions. Be that as it may, many Muslim HNWI/UHNWIs are careful when it comes to tax and succession structure in IFCs because in Jersey, for example, probate procedures vary significantly from the United Kingdom and there are no death duties, estate duty, inheritance tax or capital gains tax that is payable which is why Muslim family offices must take niche legal and tax advice from their jurisdiction before they move on to establishing holding companies and other such investment vehicles. Furthermore, although the English law stipulates that, when a deceased has passed away intestate (without a will) then the surviving spouse must receive the first 270,000 euros of the deceased's assets and belongings, excluding the deceased's monetary assets, whilst the remaining capital is equally divided between the children regardless of gender with parents not receiving anything unless there is no spouse/child left behind by the deceased. Such conditions are against the Islamic principles of inheritance but since English law allows full-fledged testamentary freedom, Muslim family offices and individuals can prevent the government from dividing assets in a non-Islamic prescribed manner.

Further to this, the regime of Inheritance Tax (IHT) in England also impacts the size of the distributable estate for heirs which is why mitigation of IHT (40% on an estate with a value of more than 325,000 per individual) is integral for succession planning. Lifetime gifting and IHT exemptions, such as spousal exemptions (100% relief), business property relief (50-100% exemption), and agricultural property relief (50-100% exemption) are also often utilised to mitigate IHT. Meanwhile, Jersey has no such IHT but rather stamp duties that are already quite low compared to English IHT. Due to such variations from one jurisdiction to another, it is strongly recommended for clients to take comprehensive legal advice for estate planning for their respective jurisdiction.

The English legal framework constructs several clauses that provide accommodating leeway for Islamic principles of succession and management to function guaranteeing both tax efficiency and legally enforced financial security for vulnerable dependants. The most noteworthy of these arrangements include the Discretionary Trust (DT) and the Flexible Life Interest Trust (FLIT) although their advantages and disadvantages depend on the legal situation.

Waqf / Trusts

Establishing *awqaf* (plural) is an admirable and very praiseworthy act in the view of Shari'a regardless of whether it is given by the rich or the poor and it need not be solely for charitable purposes provided it brings about a socially beneficial impact. The concept of trusts originated in classical Shari'a law and has been adopted by many, including English trust law with the earliest example being the statutes of endowment of Merton College which was established in 1264 as one of Oxford University's initial colleges. The statutes mentioned are said to be a translation of a *waqf*. As such, even if the English law does not specifically and explicitly cover the conditions of a *waqf*, it can certainly be established under the English trust law preferably by consulting professionals.

Foundations

Although not prevalent in common law systems, the jurisdiction of Jersey is an exception that allows foundations to be an available means for succession planning due to its pluralistic legal system. Foundations are rather corporate in nature as their councils are similar to a board of directors of a company with the difference being that a foundation's board usually consists of family members that are managing the family assets. The corporate appeal to family heads explains the popularity of foundations in the Middle East where IFCs can draft their own foundation laws and own local real estate.

Research Methodology and Findings

Gateway, on behalf of Jersey Finance, distributed a survey worldwide to gather the views of HNWI/UHNWIs, family offices and private asset managers on Islamic wealth management between June and July of 2021. The survey consisted of 190 questions regarding 8 Shari'a compliance topics: Asset Classes, Sectors, Jurisdictions, Ethical Alignment, Performance, Tax, Succession Planning and Philanthropy. The survey was closed with a total of 2,048 responses by respondents of 17 different jurisdictions with just over half (51%) domiciled in the UK and one-fifth (21%) from the Gulf Cooperation Council (GCC) countries. The respondents were predominantly (80%) in the 31-60 age bracket with the remaining 20% being above the age of 60. Of these respondents, almost 62% of them represented company treasuries, 32.3% represented multiple individuals' wealth and 5% represented family wealth.

1) Asset Classes and Sectors

In this section, the respondents were questioned on the importance of various asset classes (group of similar financial instruments) for investment decision making currently as well as in 18 months time. The measurement system provided was to allot different asset classes into 4 different classifications; Staples, those classes of high importance as of now and also in the future; Breakout, those classes with low importance as of yet but high return expectations in the future; Abating, classes with high importance as of now but predicted to taper in the future; and Laggards, those financial instruments of low importance now and the future as well.

Real Estate and Infrastructure ranked at the top in the **Staples** category due to stable returns and the asset-backed nature that is crucial for Shari'a compliance and investor security. Venture Capital, Equities, and Cash & Equivalents were also amongst Staples due to large returns and tax relief (the latter depending on different jurisdictions). Only Fixed Income was considered an asset class for the **Breakout** category most likely due to the unsatisfactory yield environment for investors recently. For the **Abating** category, no asset class was mentioned; however, multiple asset classes were put under the **Laggard** category including Structured Products, Commodities, and Crypto& Digital Assets although these classes showed more potential due to some respondents (21%) categorising them in higher categories; Hedge Funds, Art &

Collectibles, Precious Metals and Insurance-Linked Products were more unanimously considered Laggard classes.

Unsurprisingly, Islamic investors remain traditionalist in their investment strategies, relying on the security of returns that heavyweight assets like Real Estate, Equities and Cash Equivalents provide along with their Shari'a compliant asset-backed nature. It also explains investor anxiety regarding less-tangible assets such as Crypto & Digital Assets and Hedge Funds and seemingly non-Shari'a compliant assets such as Insurance Linked Products. Such preferences accurately showcased respondents' risk perceptions as 80% of Muslim investors stated a balanced risk appetite with only 16% choosing risk-taking as their dominant feature (making sure to state that they also wish to incorporate low-risk assets into their strategy). Despite the low-risk preference, the increasing importance of Venture Capital as a Staple notwithstanding the relatively short tenure of the asset class in Islamic markets does highlight the accelerating interest in the digital economy and fintech sector provided they are strict in Shari'a compliance. Furthermore, the survey presented a disparity in opinion towards Crypto & Digital Assets as one-fifth of the respondents did deem the class to be highly important in the future however the 34% of respondents who dubbed it as Laggard pulled the overall view towards the low-importance side; regardless, the potential for this class to transition to the Breakout category remains. Additionally, it was noted that the majority of respondents (81%) favour direct investments by themselves rather than indirect investments which could also explain their risk-averse nature.

2) Jurisdictions

In this section, respondents were asked to list the jurisdictions of their current investment activity and to rate these jurisdictions importance now and the predicted importance over the next 18 months; the importance categories were the same as the ones used previously namely **Staples**, **Breakout**, **Abating** and **Laggard** but in terms of the level of activity rather than returns. It is important to clarify that the response refers to jurisdictions of the investment not the domiciled jurisdictions of the investment vehicles. Results reveal that the UK was the only jurisdiction considered to be a Staple owing to its well-implemented protection of property rights and legal frameworks. ASEAN and GCC jurisdictions were amongst the top-rated Breakout jurisdictions mainly because of their Islamic genealogy; West and Southern Africa, Australasia and China and Hong Kong were also mentioned as aspiring dominions. Despite being in the Laggard category, East Africa and the United States have the most potential to transition to the Breakout category, followed by non-GCC Middle Eastern and North African countries; South Asia and Central & South America are the lowest in potential from this category. No jurisdiction was placed in the Abating category. When questioned about the importance of onshore locations for structured investments compared to IFCs currently as well as in 18 months time, using a 1-5 Likert scale, respondents leaned more towards onshore locations (3.2) than IFCs (2.9) for current investments but showed a preference for IFCs (3.4) over onshore locations (3.1) for investments over the next 18 months showcasing the former's rising popularity amongst Muslims.

3) Ethical Alignment

This section of the survey analysed respondents' views on Shari'a compliance in products and services and asked them to compare it to other ethical frameworks for wealth management and investments; this is important as a good portion of these investors use both types of frameworks simultaneously or interchangeably provided the latter type does not contradict Shari'a principles. Predictably, the majority of the respondents (62%) chose Shari'a compliant products over other conventional types regardless of poor performance whereas 48% of respondents chose solely ethical products regardless of poor performance. In terms of due diligence, exactly half of the respondents said that they did not consult internal/external advisory boards for Shari'a compliance knowledge and 46% of respondents said that they did not consult any advisory bodies for ethical compliance knowledge, with both respondent groups opting to rely on their own knowledge instead. Due to the lower percentages for both groups, there remains more potential and opportunities to be maximised if they were to seek professional advice and better consumer education. The survey also discovered a declining trend for Shari'a compliant products as the preferred framework for investment decisions with 56% of respondents agreeing there is a need for more jurisdictions to innovate and construct new ethical finance approaches beyond just the scope of Shari'a compliance, suggesting them to incorporate social impact initiatives such as the United Nations Sustainable Development Goals (UNSDGs), ESG, and UN Principles for Responsible Investment (PRI).

4) Portfolio Performance of Wealth Managers and Tax Advisors

When asked in the survey about their satisfaction with their wealth management, the survey focused on three specific criteria over the past 5 years which were the level of expertise in account management, objective decision-making abilities and the quality of client service. The overarching view (75%) was positive and respondents were content with the products and services provided to them. Respondents were subsequently given 9 specific factors for consideration and asked to rate their level of importance from 1 to 10. 6 out of the 9 were given a score of 9/10 which pertained to track records and overall reputation, know-how of international markets, asset classes and macro-economic trends, intimate understanding of Shari'a and other ethical considerations, and good relations and understanding of the client and their family's needs. Lesser importance (7.5/10) was given to criteria such as intuition, swift estimation of future market opportunities, ESG and sustainable finance credentials; though it must be highlighted that the last two factors only ranked low due to their neoteric nature for which wealth managers will understandably need more time to prepare for.

As for tax advice, 71% of respondents were satisfied in general with their tax advisors' performance for the past 5 years and when asked about the factors behind their views the variables were similar to the ones for wealth managers wherein overall reputation, understanding of international tax laws and strategies, and comprehensive knowledge of specific jurisdictions, tax regimes and asset class treatments were amongst the most important.

Less important factors included good client/family relationships and understanding, intuition, and a good understanding of Shari'a and ethical considerations though similar to the previous case, the last factor was ranked low due to it being a recent addition to tax advisor profiles.

Respondents were also asked to rank tax strategies by their level of importance; legal/company structures that allowed for better tax efficiency, asset classes with profitable tax profiles (for tax mitigation), choice of jurisdictions were ranked the highest followed by the use of philanthropy to offset tax liabilities, seeking OECD and EU compliant jurisdictions for Transparency and Information Exchange protocols and the lowest-ranked strategies being gifting and transferring wealth to the family for tax allowance maximisation; the last strategy's rank being the lowest is rather curious considering the majority of respondents belonging to the jurisdiction of the UK though this may be rationalised in the context of the low thresholds placed by the British government.

Succession Planning

In this section of the survey, respondents were inquired about their objectives and concerns with succession planning, use of trusts, *awqaf*, and foundations in succession, and preferred jurisdictions. The most notable response was that 96% desired their heirs to inherit their wealth, with 36% already taking the appropriate steps to secure their succession and the remaining 60% in the process of doing so. The gargantuan opportunity for wealth management and jurisdictions to capitalise on these upcoming wealth transfers can not be understated over the coming years. Of these respondents planning succession, 57% stated that they plan to take tax advice and 63% plan to take Shari'a compliance advice whilst only 32% have tried using *awqaf* in their planning strategies though 99% of them have expressed positive reviews of it.

The fact that 63% of the surveyees plan to consult Shari'a advisors even though 50% stated they rely on their own knowledge may seem contradictory however this phenomenon can be explained by two reasons; either their selected jurisdiction has a minute tax impact on them or they realise that the Shari'a component of their succession planning is more intricate than they realise due to which they find it necessary to level with their personal values. Resultantly, families will seek jurisdictions that are compatible with Shari'a principles and investment structures and offer professional quality advice and management services. To this extent, Jersey is a prime example of such jurisdiction with abundant Shari'a compliance resources. Additionally, Jersey Courts emphasise their decision to not implement foreign judgements that may jeopardise wealth protection and succession structures offering families reassurance that their heirs and beneficiaries will be protected and that the testator's wishes will be honoured.

In the survey, 76% of respondents shared that trusts are an important aspect of their succession planning and the top 5 most favoured jurisdictions to conduct their affairs are Jersey, the UK, Dubai International Financial Centre (UAE), British Virgin Islands (BVI), and Malaysia. On the other hand, only 30% of the respondents stated that they have looked into foundations for their succession planning, listing the DIFC (UAE), Jersey, the UK and Cayman as their most favoured jurisdictions for foundations. They further noted that Jersey is more preferred by families looking to retain control of assets without transferring them to a trustee; this is because in Jersey a

foundation is managed by a Council wherein it is mandatory to include a 'Qualified Member' who is an individual tasked to regulate and oversee the decisions of the Council. If a family wishes to not include an outside member, this role can be fulfilled by a Guardian, a role that can be taken up by the founder themselves. Furthermore, foundations in Jersey are given the option to employ subsidiary companies to manage tasks for the family such as conducting philanthropic activities on their behalf. This is important as philanthropy may be utilised by families as a strategy to hold on to "wasting assets", assets that may depreciate over time, as they would not be of value in trusts. Lastly, when asked about the primary concerns they may harbour regarding succession planning, most respondents noted that they were most worried about the smoothness of the transition of inheritance and potential infighting within the family that may jeopardise the family unity. Other concerns included retaining wealth in the family, generating profit on the wealth for future generations, and prevention of wealth misuse or misplacement.

Philanthropy

Regarding views on philanthropy and its significance, 96% of respondents asserted that it was important for them to ensure they engaged in philanthropic activities and 79% further stated that they had already made significant contributions with the intent to continue doing so. 83% also added that it was meaningful for them to give charity in line with their faith. On the question of the portions of wealth to be given in philanthropy, the results were more mixed. The consensus of 67% of the respondents was that anywhere between 10-50% was a fair amount, with 37.1% choosing between 10-25% and 29.9% choosing to donate 25-50%. 10.4% desired to give over 50% with 7.3% even claiming that all their wealth should be given to charity.