The Role of Islamic Social Financing
in Achieving the Sustainable Development Goals Dialogue
Seminar Discussions

Topic	**Challenges of Islamic Social Financing and UN Mechanisms**
Seminar Lead/Support	SASG/ESCWA/IsDB
Language	English & Arabic
Summary	This seminar will focus on the specific challenges faced in applying the mechanisms of implementation for Islamic social financing within the UN system.
Participants	A diverse audience of individuals relevant to the Global Sustainable Development Agenda is targeted, including senior government officials, potential investors and beneficiaries, development partners, international and national civil society organizations/NGOs, private sector, philanthropists, foundations, think tanks and academia.
Objectives	• To present challenges facing implementation of ISF within UN mechanisms • To discuss how to overcome those

1. Background Information[1]

Zakat still needs to be better captured, harnessed and channelled to respond effectively to the SDGs. In Islam, zakat and alms-giving is accompanied with humility. It is emphasised that to do good with wealth is better than ostentatious display, which has no social value. In practice, Muslims commonly channel alms through informal structures, giving directly to beneficiaries or using mosques and local charities or organisations to disburse contributions to those most in need. Such giving is not ordinarily recorded in official systems. Additionally, if one gives zakat to family or friends, this will not be captured. As a result, knowledge around levels of wealth in Muslim societies is low, especially amongst high net worth individuals as an individual's net worth can be calculated according to how much zakat they give (2.5% of cumulative wealth).

As zakat can be given directly to beneficiaries, it is difficult to calculate accurately its magnitude and impact. As long as zakat distribution remains sharia-compliant, there is scope to align its expenditure with development objectives. Until recently, zakat directed to international development was not commonplace but today this is changing. Indeed, this can happen through national zakat agencies, international organisation platforms that capture zakat, or through the work of civil society organisations:

- A number of Muslim-majority countries, including Qatar, the United Arab Emirates, Indonesia or Malaysia, have zakat agencies that operate as a part of government. They collect zakat. Ordinarily this is done to meet domestic needs and good practice examples can be seen in Malaysia. Malaysia's method of zakat collection highlights how a government can efficiently administer this important function and deliver on

[1] This background is taken from "How Islamic Financing Contributes to Achieving the Sustainable Development Goals," *OECD Development Policy Papers*, 30 (June 2020).

behalf of citizens. However, not all Muslim-majority countries have introduced the system of zakat, which is considered a private activity, thus making it difficult to assess its effectiveness in poverty alleviation

These agencies do not always operate internationally but could do so through an international window, integrated within the country's development co-operation activities. Indeed, this is the case of Indonesia where activities, including scholarships, humanitarian aid, refugee support, food aid, and co-operation related to peace and security, are delivered with zakat funds to other countries through its National Amil Zakat. Another example is the United Arab Emirate's Zakat Fund, which can disburse funds for domestic donors to implement projects abroad.

Official zakat-giving requires improved organisation, notably to enhance trust in where funds go to and how they are spent. Donors could promote the development of vehicles or even institutions that allow Muslim individuals to make charitable donations in a way that speaks to their religious belief. This could contribute to a better allocation of global financial resources for development, both official and private sources. The initial costs of setting up such institutions and creating an enabling environment for these to operate could be high. Appropriate legal, fiscal and banking safeguards would need to be introduced to ensure compliance with sharia and to ensure trust of Muslim citizens.

If zakat is to deliver on development goals, it is critical that current flows are better recorded. Since amounts given in zakat are expected to grow, it is only through better accounting of these flows that the full power of zakat can be harnessed. In some regions, further awareness on zakat could also be a useful way to leverage this financial resource for development, notably in Sub-Saharan Africa where capacity and awareness are low.

Waqf, or the plural Awqaf (used interchangeably in this paper), mobilises large amounts of private and public finance in Islamic social finance. The waqf is an effective means of distributing wealth to a community and persons over a long period of time. This can translate into providing social infrastructure, such as housing, basic infrastructure, schools or hospitals. Despite limited data on awqaf, a recent estimate of potential awqaf in the case of Indonesia shows that it could generate up to 0.85% of its GDP.

Awqaf generally work effectively in providing public goods to a population but their application in a development context has been limited to date. There are a number of issues where reform would make them an attractive financing tool for development. Indeed, the management of these funds often generates low social returns. In the United Kingdom, preferences for giving to charity (obligatory zakat) rather than investing in awqaf has reduced the prevalence of this financial instrument, because the instrument as a whole has not been delivering high-value social benefits. However, the United Kingdom is well placed to demonstrate how awqaf can contribute to sustainable development, in particular to understand when its use can generate financial and social returns. This finding also aligns with recent growth in social impact investment, which is looking to achieve strong social returns and high levels of social impact.

Whilst awqaf offer consistent returns, stability and predictability, a major hindering issue has been that investments are made in perpetuity and so there are limitations around how easily money can be divested and how actively funds need to be managed to generate returns. Investors traditionally look for mechanisms that mobilise finance and in turn deliver a positive return. By having endowments that offer little flexibility or control to investors, there are few incentives to encourage stronger investment. Many of the waqf assets in existence have conditions from the original donor, which remain in effect in perpetuity (and many awqaf have been in that form for centuries). The religious nature of these restrictions makes modifying the purpose difficult, without significant reputational risk for the waqf trustees.

As such, establishing high-profile awqaf, with strong social returns and high levels of social impact, can increase both the appetite for more risk-averse investors to engage with this financial instrument. The IsDB has invested heavily in developing and delivering awqaf effectively since 1979. The different awqaf funds that the IsDB manages respond to a number of development challenges and highlight the significant financial resources that can be mobilised through this channel, sometimes combined with other financial instruments. For example, the IsDB's Special Fund for Poverty has secured commitment from OIC member countries and other donors to resource a USD 10 billion fund which taps into domestic awqaf, amongst others for the purposes of poverty reduction. These funds are usually used to finance the construction of buildings in waqf lands, real estate development projects to enhance existing waqf buildings and increase income assets, to support social activities, notably in the field of education or health over long periods of time. The IsDB also manages the Awqaf Properties Investment Fund (APIF), which is dedicated to financing revenue-generating awqaf projects globally.

2. Agenda/Format

Moderator TBD 90min

		Speaker
1min	**Welcome**	*Moderator*
5min	**Background**	*Dr. Ahmed Al Meraikhi, Special Adviser to the UN Secretary-General*
xxmin	**Challenges of ISF Implementation**	*Dr. Mohammed Abdulla, Habib Bank AG Zurich*
xxmin	**Challenges of UN Mechanisms**	*TBD*
xxmin	**Exploring Modern Mechanisms with Respect to ISF**	*Dr. Rushdi Siddiqui, Azqa Capital*
xxmin	**UPDATE**	*Dr. Mohammed Obaidullah, Islamic Development Bank*
	Discussion	
40min	**Lead by the moderator**	
5min	**Closing**	*Dr. Ahmed Al Meraikhi,* Special Adviser to the UN Secretary-General

Dr. Sami Ayoub, University of Texas

3. Additional Information

https://www.sdgphilanthropy.org/index.php/system/files/2020-07/OECD_Islamic%20Finance.pdf

DIALOGUE ON
ISLAMIC SOCIAL
FINANCING
AND THE SDGS

IsDB