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Economics of Philanthropic Institutions, Regulation and Governance in Turkey

Mehmet Babacan[♦]

Abstract. This paper merges the literature on regulation, specifically private provision of public goods, and governance with the literature on philanthropic institutions (*awqaf*) in Turkey. Traditionally, *awqaf* (plural for the *waqf*) have been very functional regarding the socioeconomic realms in Muslim societies. On the other hand, the provision of public goods is one of the core discussions under the literature on regulation and governance, particularly the property rights. This paper analyzes the role of *waqf* which has historically been more than a charitable organization: an economic agent in Turkey. Being a long-time provider of public goods, *awqaf* can be studied of property rights and regulation process, while its organizational structure could be considered as a subject to the firm theory. Turkish philanthropic institutions possess historical significance in terms of their organizational evolution and relationship to the changing governance structures in the country. Therefore, also discussed in this paper are the similarities and differences between the *awqaf* and Western charitable organizations, particularly in terms of organizational structures, definition of property rights, and their evolution under different governance-related structures such as rule of law and contract enforcement.

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1. Introduction

For centuries, philanthropic institutions have played an important role both in Western and Islamic traditions. A specific organization called *Al-Waqf* has achieved a significant socioeconomic position in the Islamic world that is comparable to its counterpart in Western societies. Functioning beyond private philanthropic institutions, awqaf (waqfs) possess a wide range of contributions to social welfare.

Al-waqf literally means to stand, to allocate, and to immobilize (to make dependent and conditional). Both in Arabic literature and religious law, it refers to a special type of donation in which the donor is not the beneficiary of the revenues, and profits stem from the assets donated. In the pre-modern history of the Islamic societies, usual types of the waqfs are the family waqfs. They aim to make ongoing revenue sources for the descendants and their lineage. Such an endowment is characterized as being *mu'awqqab* (for a descent group). Since waqfs are based on interpretation of the Prophet's *hadith* (words and deeds), this judicial attempt is also driven by the social and economic complexity of Islamic society along with the religious motivation behind them.

With the expansion of Islam throughout western Arabia, Northern Africa and the East (Iran, Afghanistan and India), Islamic societies became even more developed and sophisticated. In the early Islamic period under the rule of Umayyad and Abbasid dynasties for instance, Muslims tried to answer the needs of this complex social structure. Therefore, early examples of awqaf (with its judicial grounds) are observed in the first and second century of Islam. The finance of the *jihad* (struggling for God's sake) is considered as an important motive during the early periods of the Islamic state [quoted in Gil (1998)]. Therefore, chief function of the waqf was to finance the Muslim fighters for the Faith and for the early Muslim brotherhood. It was a benefaction for God's sake without seeking any worldly reward. Later periods of whatever the motives are, the waqf institution has played an important role in Islamic societies as it was both common and economically significant. In the example of Ottoman State's classical age for instance, it is quite impressive to witness how comprehensive and common are waqfs and their properties in the Turkish society. These properties once constituted one third of the cultivatable lands in the Ottoman State, including the Middle East and the Balkans.

Some scholars view founding a waqf as circumventing Islamic law, as there is no direct evidence from the Qur'an, only interpretations of Prophet's

hadith. Since all the property owned by individuals was subject to taxation, people could be said to have some “property rights” acquiring motives in order to protect their heirs, and in some cases themselves. It should, however, be noted that most of the waqfs founded through Islamic history are charitable foundations rather than family endowments. Therefore, Muslims’ main motivation for founding an endowment is more than simply circumventing the Islamic law. Simply put, waqf prevailed as a private provider of public goods and services until the modern type municipalities were founded in 19th century Islamic world, specifically in the Ottoman State.

Provision of public goods and the definition of property rights have been a challenge for every society regardless of their development level (Kuran, 2001). Public goods are defined as goods that are non-excludible (not requiring special authorization to consume) and non-rival (to be consumed by many of the demanders at the same time). Waqfs, acting as intermediaries between localities and the central government which produced public goods, should also be analyzed with regard to the Islamic countries’ economic development and their adaptation of global governance bodies. A private institution (i.e. waqf) can supply any good or service that is defined to be public in an efficient way, even if it creates an incentive for monopolistic behavior in some cases. Due to the issues regarding economies of scale in provision of such goods, government intervention might even lead to losses in social welfare. However, it is argued that under the private provision of the public goods there may still be some need for government regulation of market functioning and maintaining competition (Kahn, 1988).

For the aim of this paper, historical significance or the “history of waqf system” is not the main question. We will only provide a discussion of the waqf system in regard to modern regulative and governance structures and try to answer whether this institutional basis is an obstacle on the development of advanced social and economic bodies. Regulations on the provision of public goods constitute the first dimension of the relationship between the waqf institutional base and modern governance structures. This can be described as the positive analysis of the waqf system in terms of regulatory issues, such as principle-agent problem, monitoring, and adverse selection. The second discussion with that regard focuses on the normative arguments (such as Kuran’s arguments) around the waqf system. The normative arguments against the history and role of the waqfs define such institutions as a result of inadequate governance structures and the lack of secular law practices in the Islamic world. Accordingly, waqf system

emerged in those societies which lacked well-defined property rights or a functioning democracy and rule of law. Additionally, this is said to have granted an excessive role of government bureaucracy and thus led to high levels of corruption (Kuran, 2007 and 2011). Our argument in the last section of this paper however contends that the long-prevalence of waqf system in the Islamic societies could not justify such normative arguments as put forward by Kuran and others. Historically, those institutions played a complementary role to the government's provision of public goods, with both rises and falls throughout the mediaeval and early modern ages of the Islamic world (especially Turkey). Their counterparts (i.e. western charitable organizations) have also prevailed for centuries in other societies that demonstrate well-defined governance structures. For instance, recent figures on the waqfs established in Turkey after 1980s clearly indicate the rise of waqfs is not associated with the decline of governance bodies in a society. Rather, they play a complementary role to the government policies regarding their social dimensions.

The structure of the paper is as follows: The first section provides a brief definition and a perspective on the historical development of waqf institution along with its organizational structure and different types. The second section focuses on the economic and social role of waqf in the Ottoman and modern Turkish society. This section draws special attention to the issues that arise from agency problems while elaborating on the reasons that led to inefficiency and corruption. Third section of the paper elaborates on the reasons for the decline of waqf system and brings light to the centralized waqf system and the effects of government regulation in Turkey, while adapting an institutional perspective on the possible correlation between the evolution of governance bodies and recent developments regarding the waqfs in Turkey. Last but not the least, in the concluding section; this study argues that waqfs are complementary bodies to modern governance structures rather than being alternatives or obstacles to them.

2. Foundations and the History of Philanthropic Institutions in Islamic Society

Waqf as a philanthropic institution finds its roots mostly in Islamic heritage. Beginning with the early stages of Islamic social and intellectual life, the perception and belief in the "*day of judgment*" made Muslims forming institutions or performing pious deeds. The thought of being rewarded in the life hereafter has led them to seek everlasting good deeds, which were believed to please God. Religious factors draw the limits of such an

organization, as they are the basic motive in founding a waqf. It is a voluntary, permanent, and irrevocable dedication of a portion of one's wealth to God, while the corpus of the waqf should remain intact because it belongs to God (Ariffhidayat, 2010).

2.1. Conceptual and Organizational Aspects

The definition of waqf is not uniform across Islamic society, although there are basic forms that do not vary within different types of waqfs. A waqf is usually defined as an unincorporated institution established under Islamic law by a living man or woman for the provision of a designated social service in perpetuity. Emphasizing religious factors beneath, the waqf can be defined as an action of a Muslim individual, motivated by an element of Islamic culture, to transform some or all of his personal assets into pious foundations to serve the public.

Waqfs can be categorized based on their waqfiyyas (endowment deeds):

1. Charitable waqfs are founded for the provision of social and economic services. The beneficiaries of this type of waqfs are usually the poor, the elderly, or people living around the holy mosques of Mecca, Medina, or Jerusalem. These waqfs play a significant role in sharing the central government's fiscal needs and the responsibility for provision of public goods.
2. Family waqfs are typically the ones which the founder states the beneficiaries to be his/her descendants and continuing lineage. These are mostly founded to ensure the property maintains perpetual revenue for the founder's family after his/her death. A family waqf prevents the government, for instance, from confiscating the property appropriated as waqf.

A family endowment (waqf) can be established between two living beings *inter vivos* (Powers, 1999) or by last will and testament. This type of endowment is not limited by size. An *inter vivo* endowment immediately takes effect and cannot be revoked by the founder. A testamentary endowment takes effect after the founder's death and is limited by one-third of the person's net assets. This is a legal constraint on many Muslims. Another implication of this type of endowment should not be in favor of a legal heir of the founder. Property of an endowment were becoming perpetuity, by designating a religious institution such as a mosque, school or

the personnel associated with the institution as the ultimate beneficiary. The endowment deed and other important records relating to the waqf are important to avoid future disputes, or at least make the judiciary power to solve the issues.

Although there are some views that contend the origin of waqf (see Kazıcı, 2003) was from the Roman, pre-Islamic Arabia or Byzantium era, there is no sound evidence to support this. Additionally, the level of interactions between the civilizations is subject to another study, and these discussions will be discarded for the aim of this analysis (assuming the waqf institution was born with the introduction of Islam). In the formation of waqf, there were two legal principles that Muslim jurists identified:

1. The distinction between real property (*asl*) and the revenue or usufruct (*manfa'a*) generated by that property;
2. The notion that real property could be sequestered in perpetuity [quoted in Powers (1999): Gibb and Kramers (1965)].
- 3.

2.2. Early History of and Motives for the Waqf

Although the Qur'an does not mention or specify any institution called waqf, many verses are interpreted as instructing Muslims to establish such foundations to serve as charitable organizations for the Islamic community. The waqf helped the Islamic State to provide public services and goods that used to be mainly financed by the *zakat*, later followed by taxes collected from believers, and the expropriations from non-Muslims. The judiciary form of the waqf was established around year 755, during the 2nd and 3rd Islamic centuries, according to the sources quoted in Kuran (2001). This implies the early Islamic state was capable of providing public goods because the community was not so large in population and complex in terms of organization. It is assumed a central organization would function more efficiently in such a society. This brings to light the "worldly" motives for the foundation of the waqf institution. First to be considered is the transformation in the structure of wealth held by the Islamic community. In the 7th century Arab world, most assets were composed of movables at the hands of merchants and herdsman. However, during the period of Umayyad and Abbasid dynasties (661-750 and 750-1258, respectively) most wealth consisted of immovable assets, such as agricultural land and real estates. One of the most significant aspects of a waqf is the endowment to be immovable. The Zakat system and the after constituted waqf system would have different impacts on different social classes. In the early years of Islam, most of the

wealth was in currency form and thus it was exempt from taxation. As the Islamic society developed in size and complexity, the waqf system allowed the founders greater security of their property and reduced taxation. Individuals would enhance the protection of their wealth, and the waqf would guarantee the provision of the public good/service (if the property appropriated was for public serve).

There seems to be a contradiction between two functions of the waqfs since provision of public goods could be considered as a limitation on personal wealth. However, legitimacy of the waqf institution is based mostly on the public goods it provides. This is considered an implicit contract (Kuran, 2001) between the founders of these institutions and the ruling government. The function and mission of waqfs were accomplished under the rule of Prophet. While rulers of the Islamic State encouraged foundation of waqfs, which meant a serious reduction in the tax revenues, they knew these organizations to provide public goods in a decentralized manner because of this implicit contract. This condition also legitimized the government. This motive was observed mostly in the ruling class which also held most of the wealth. They found waqf as a means of protecting their personal wealth, as well as a means for maintaining legitimacy because the waqf institution was an efficient tool for both providing public goods and developing religious organizations for which the society was sensitive. There are many instances in the history of Islamic societies that implies the waqf is to be attributed as a great importance. In many cases until the attempts towards centralization of waqf system began, these institutions were protected in a strict sense so that even judiciary power could not make any changes on or decide to confiscations. Waqf system developed in pre-modern Islamic mid-east, including Iran, and in southeast, India to a high level which made estimations on the land they possessed to be almost one-third of the total in most of the Islamic states. As previously stated, waqf system is based on land and other immovable properties as well as movable properties. By means of the waqf system, personal wealth was transformed into social institutions functional within an Islamic society (Yediyıldız, 1996). Mosques as religious, political, and cultural centers in Islamic cities were mostly founded and financed in their operations by waqfs. Within decades, mosques were expanded to schools, hospitals and other social institutions. These institutions facilitated the social interaction and avoided possible stratification, especially in small towns. Some of the remaining buildings or complexes from waqf systems are still functioning around the Islamic world today.

3. Waqf System in Turkey: From Provision of Public Goods to Economic Decline

Religious and secular motives for founding a waqf are described in the previous section. The discussion in the second section will first focus on the economic significance and social role of the waqf system under a state-controlled economic environment. Factual and possible reasons which led once well-functioning and decentralized waqf system to become mismanaged, inefficient (even corrupt) and then centralized, are discussed in this section. Theories of property rights and principle-agent problems have a lot to do with the waqf system regarding the organizational structure of a waqf and potential welfare costs. Provision of public goods is another ground that unarguably makes the waqf system a question of regulatory economics.

3.1. Economic Significance and Social Function

Waqf appears to be the most dominant economic actor outside the government in the Islamic States. After the early periods of Islam, significant shift in economic activities from mercantilist trade toward agricultural land-based static systems increased the importance of waqfs. Non-arguably, waqfs had their most significant economic implication in the Ottoman world. In the early 18th century for instance, the total waqf land were nearly one-third of the productive land in the Ottoman State. Waqfs used to possess many different immovable assets, such as shops, residences, production facilities, and other social/public facilities. Since most of the waqfs founded by the ruling elite in the case of Ottomans, they possessed a large amount of property and wealth, they easily provided public goods under governmental supervision. The economic significance of waqfs had two dimensions: 1) provision of public goods and 2) protection of property rights. While some waqfs directed or supported provision of public goods, others provided private goods that are excludible and rival. Tax relief could be given as an example to the latter. There are many different examples of non-rival consumption goods provided by waqfs, such as delivering water to a local area, paying a neighborhood's taxes, defending a town, supporting retired sailors, and operating commuter ships, among others [examples are drawn from Kozak, 1985, quoted in Kuran (2001). Many of them could be found in also Barkan & Ayverdi (1970), Yediyıldız (1982;1984) and Kazıcı (2003)]. Waqf system is observed to be the primary "vehicle for financing Islam as a society" (Hodgson, 1974), quoted Kuran (2001). An important social service provided by the waqfs was the foundation of schools. In the Ottoman period,

after conquering Constantinople (Istanbul) until the 19th century, the number of the *madrasahs* (schools for higher education) built by the waqfs totaled more than 500 (Kütükoğlu, 1977), Kazıcı (2003) quoted. Along with the services they provided, these schools usually financed their own expenses. During the Ottoman period, even a lighthouse on the Romanian coast was established under the waqf system and was treated as a pure public good to be provided by the government from tax revenues. The waqf system constituted a third fiscal category beside the state treasury and “timar system”, which was based on taxation of revenues (mostly agricultural) from land.

The waqfs were under protection of religious law, therefore courts mostly decided in favor of the founders whose will was respected according to the endowment deeds. The right of founding a waqf was granted only to Muslims in an Islamic State. However, there were minor exceptions to this general rule for the Islamic State. This exception sometimes granted the right of establishing a waqf by influential Jewish and Christian individuals. In the 19th century, this rule was eroded with the permission to individuals of other faiths for establishing a waqf. During the period Christians and Jews were granted the right to establish a waqf, they gained significant economic ground against Muslims in the Ottoman State. It would appear that the “worldly waqfs” transferred income from politically and militarily dominant Muslims to non-Muslims (Kuran, 2001), since the non-Muslims were also exempt from taxations that Muslim individuals were subject to. The implicit contract between the government and founders in the process of founding waqfs are already discussed. Another issue which arose is the truthfulness and credibility of a waqf. Because there is a great amount of resource allocation by the waqf system, the credibility and monitoring problems are important to consider. A waqf obviously acquires validity and credibility in its operations by religious piety. The monitoring issue was in fact easy for the charitable waqfs, rather than family waqfs. Since most of the operations undertaken by the former ones were public, any disputes over the function of the waqfs, or the allocation of revenues, would quickly be a subject of court decision. The family waqfs were hardly monitored and any disputes over them would be more controversial, compared to the charitable waqfs while in some cases the beneficiaries had the cause to sue the mutawalli over their actions. The endowment deed, which is basic of a waqf, could be either destroyed or damaged so that the courts hardly took action against the status quo. These problems caused most of the family waqfs to be confiscated by

the government, more intensely after the establishment of the new republic (in Turkey).

With the wealth sheltering function of the waqf, a person could avoid heavier taxation (beyond the limits of zakat system) on his/her revenues and property (based on the Ottoman land system). It is often claimed that this motive was fueled by the fact that the “Islamic world never developed effective safeguards against opportunistic taxation or expropriation” (Kuran, 2001). This argument is only plausible to a limited extent since Islamic law had a solid ground for protection of individual rights. At times however, given the authoritarian governments in power, the rulers could expropriate the private property for the sake of the *ummah* (term used mostly for a Muslim community whatever its level of development, a conception from Qur’anic verses) and/or State. The mutawalli, being responsible for the management of the waqf, received 10% to 15% or more from the revenues generated where regional norms allowed. Usually by subjective interpretation of the endowment deed, they defined the social obligations of the waqf conservatively. The mutawalli had extensive authority on the use of revenue under the constraints of endowment deed.

Individuals founding family waqfs had limited social obligations and thus, limited economic functions. Hence, while waqfs were eroding the tax base for the government, the least desirable cases were to be family waqfs because they did not provide many social goods or involve economic activity. According to one view, weak property rights (of individuals against State) and restricted testamentary rights according to Islamic law (Kuran, 2001) are the basic economic motives of founding a waqf. Following the same presumption, one could argue that the State was restricted and committed to uphold private property rights under the sacredness and protection of the waqf institution. This argument is, however, confronted by the fact that government regulation has been excessive on the waqf institution during times of institutional decline in Islamic societies. Therefore, aside from the positive arguments around the need for regulating the waqf system to eliminate issues (such as agency problem or monitoring), the above normative arguments on the governance-related motives for waqf institutions become obsolete by historical facts of Islamic societies. An even more important point is that Islamic law was not that static to prohibit the evolution of waqfs and it was indeed very much flexible to allow the waqf institution to evolve over time. As Çizakça (2000) puts forward the ten conditions of Hanafi jurists regarding the waqf endowments, it is quite obvious that foundation and management of waqfs are dynamic processes that could adapt into different environments in time.

As stated above, the major advantage of the waqf system is the polycentric structure of providing social services, including public goods. A decentralized system made communication and co-operation among different entities easier and thus worked efficiently. One issue regarding the locality of waqfs is harmonization and well-functioning. Local institutions made information costs lower, given the “local knowledge” of communities, families, individuals, and customs implied waqfs to be local agents of government. There was uniformity in the system which led to the co-operation between waqfs and government. However, this introduces the issue of flexibility of the waqfs regarding 1) their foundational aspects, and 2) operational aspects.

3.2. The Structure of Waqf System and Factors Leading to Economic Inefficiency

Although the waqf gives a broad freedom to the founder, it is limited in terms of operations and management. The mutawalli is first restricted by the endowment deed, which is represented by static perpetuity, and second, the managerial flexibility is limited because their actions are under the court’s monitoring. Perhaps because of this potential inefficiency, the founders of the waqf system made the residuary mission of every waqf to the benefit of the poor. This mission is once argued to lead the formation of a large class of indolent beneficiaries which was a factor behind Islamic world’s long economic descent (Quoted in Kuran (2001): Akdağ, 1979; Cem, 1970). As a counter argument, however, waqfs are usually seen as complementary to the public services where in many cases, they have increased operational efficiency. Although a waqf is to be perpetual, in some cases the mutawalli could use waqf’s revenue stream for a temporary mission, such as helping the victims of natural disasters. A mutawalli was however limited with only one set of changes on the operational functioning of the waqf while in some cases the endowment and waqf’s mission were also subject to changes. The judiciary power was also effective on the managerial decisions of the charitable waqfs such that even there were special judges (*kadi*) and courts for waqfs in Istanbul, Bursa and Edirne (three capitals of the Ottoman State (Öztürk, 1995).

A similar argument against the waqfs is made on their sources of inefficiency. Accordingly, the root cause of operational rigidity can easily be identified as the supremacy given to the founder’s rights to set the terms of management in the traditional waqf system. This situation makes the

mutawalli only an executor of his or her decisions, suggested by Kuran (2001). The mutawalli is argued to be only allowed to make interpretations of the understated or ambiguous parts in the endowment deed. Thus, following the same logic, waqfs are considered to remain perpetual despite having a static structure which made them operate inefficiently and incur substantial losses for centuries. Given that assumption to hold true however, it leads to the question of how such static institutions managed to last for centuries. The answer is not clear, of course. It is also observed that constraints on the mutawalli have been gradually removed by re-interpretation of court decisions among different provinces of the Ottoman State.

In the case of charitable waqfs, the extent of operational rigidity arises because of potential agency problems. In cases where the mutawalli is not allowed to make modifications or changes in the mission of the waqf to ensure the honesty and reputation of the institutions are protected. The rights of beneficiaries stated with the endowment deed were also guaranteed. The founders usually try to prevent potential abuses in the use of property appropriated for a selected mission that the mutawalli is forced to operate under tight rules according to Kuran (2001). However, the case of 'ten conditions' on endowment deeds and mutawalli's operations again provides a solid ground to assume more flexibility than suggested by Kuran and others (see Çizakça, 2000 and Çizakça, 2010). Despite the pros and cons regarding the waqf system, one should still consider that the classical waqf structure was shaped by the socio-economic and religious perceptions in the middle ages, so the organizational and operational structure might not have allowed them to make fast adjustments despite the fact that they witnessed long-term changes.

3.3. Waqf Management in Practice and Rise of Corruption

The discussion on operational flexibility of the waqfs is based on these institutions' compatibility with the economic changes and development. It is observed that founders did occasionally give broad powers to their mutawallis. Their eyes on the overall value to be maximized, the founders would leave the waqf only under judicial review, if necessary. The usual inflexible operational aspects of the waqf system could also be said to lead the officials sometimes shirking their responsibilities. The mutawalli, employees, and judges have tried to make pragmatic adaptations under the founder's directives. Founder's control over the waqf's management, however, usually seemed to erode, especially beyond his or her lifetime.

This would often occur when the waqf deed suffered damage or disappear with the passage of time (Kuran, 2001). In such cases, the courts mostly modified the operational functions of the waqf in favor of the beneficiaries or the wider community. The judicial or governmental intervention could be viewed as a form of regulation on the operational flexibility of waqfs. Although there is evidence that mutawallis exploited the ambiguities in the endowment deed in terms of operating the waqf, it does not prove the institution operated under optimal flexibility (Kuran, 2001). Inefficiency was either a result of shirking at managerial and operational level, or in some cases constraints from the founder's directives. Charitable waqfs were also subject to complaints about their social duties and they would face with undesirable court decisions. Individuals with little stake in the foundation of a waqf often considered their private benefits only or social services and goods produced by the waqf, regardless of their economic implications for the institution itself. They constituted another constraint on the operations of the waqfs. In family waqfs for instance, the beneficiaries would file complaints in order to find evidence of wrongdoings in operations and management. This condition of uncertainty led the mutawallis and employees to exercise caution in introducing change. Disputes over the operational flexibility could result in court decisions either to be welcomed by the mutawalli giving the opportunity of transformation without the founder's blessings, or blocking necessary changes even if they are in favor of the founder.

There are conflicting views over the causes of managerial and operational inefficiencies in the waqf system. Following the neo-classical and new institutionalist approach, one could easily regard the waqf system as the "bad" that led the economic realm of Islamic societies to collapse over time. In Coasian terms for instance, the waqf system is argued to bear a lack of well-defined property rights in practical terms. Since the judicial interference to the operational flexibility and inconsistencies among the decisions discouraged the managers, transactions cost, the possibility of shirking and post-contractual opportunism increased. As previously stated, there is an implicit contract between the State and waqfs in general. Another dimension is the implicit contract between the mutawalli and the founder enforced by the endowment deed and judicial system. The transactions cost, on the other hand, was too high in most cases because of the uncertainty of the result of taking an action by the mutawalli. The transfers of rights on the property, or even renting, were always under constraint of the waqf deed. Many court decisions do not show the transactions cost of actions taken by the mutawalli in order to change the operational aspects or re-interpret the

missionary statements in the deed. Because of anticipated transactions costs, it can be argued that a large number of socially desirable or efficient waqf transactions and adaptations must have remained unimplemented (Kuran, 2001). The lack of well-defined property rights in the waqf system operations and high transactions costs are regarded as the root causes of inefficient management and tendencies toward corruption in each level; mutawalli, employee and the beneficiary, especially during the times of war and other social and governmental difficulties. Managerial inefficiency made the resources to be allocated either excessive or insufficient. The provision of private goods was preferred over public goods because of the misaligning incentives. Although the religious sentiment would have alleviated the temptation to shirk, it could not have kept waqfs permanently efficient (Kuran, 2001). This statement could be supported with adequate evidence of poor management in the practice of waqf system. Despite the positive arguments on the reasons for the decline of waqf system due to the operational issues regarding individual waqfs, it is not quite evident that such charity organizations systematically suffered from bad governance practices and in turn led to persistently insufficient institutional structures in Islamic societies.

4. Response to Economic Decline: Evolution in the Waqf System

In sum of the institutional and practical approach towards the waqf system, the terms “stronger the state; weaker the waqf system” would be the best motto to describe what happened within the last two centuries of the Ottoman and Turkish states’ history. At the dawn of the 19th century, the waqf system was suffering from irregularities and inefficiencies in administration, both of which weakened the legitimacy of these institutions. Misallocation of resources and the failure of transformation in operational aspects led the waqf system to breakdown. The pecuniary motives of the founders and mutawallis, which led to big rents from the operations of waqfs, were legally questionable. Government provision of public goods was another factor causing the waqf system to loosen.

4.1. Centralization and Regulation of the Waqf System

The evidence of thoughts on centralization of the waqf system goes back to 1630 when an Ottoman advisor to the Sultan, Koçi Bey ([1630], 1994) urged the Ottoman State to take the control of waqfs established on its territories (Kuran, 2001). He argued private individuals acquired state lands under the institutional protection of built-up awqaf. Contrarily, a 16th century

intellectual and statesman, Aşık Paşazade, directed serious criticism against the attempts of abolishing several waqfs (Çizakça, 2000). As time passed, sultans managed to assert control over vast waqf properties that had turned them into low-taxed, if not tax-exempt, private property (Kuran, 2001). For years, however, resulting confiscations by the State left the traditional waqf system intact. While having respect for and being tied to the founder's will on the individual waqf itself, Ottomans brought some innovative measures to the waqf system, such as centralization under a higher authority. The first effective step towards centralization of the waqf system was the establishment of the State Ministry of Waqfs (*Nazareth of Awqaf ı Hümayun*) in 1826. After the "beneficent administrative reforms" (*Tanzimat-ı hayriyye*) in 1839, the rulers' rapprochement to waqfs was relatively challenging to the structure of the traditional system. Although first observed in the larger cities and the capital city, there was a fast movement towards a gradual centralization in most of the Ottoman provinces. An example is the effective regulation of charitable waqfs in Egypt. All lands belonging to existing waqfs were formally nationalized in 1812, given that Egypt was autonomous in effect. Following the Ottoman Land Law in 1858, Christians and Jews were encouraged to found waqfs which would effectively a part of the central governance of the waqf system (Shaham, 1991). The decade of the 1860's were observed as the period of big projects undertaken across the Ottoman territory which required vast financial resources to be steadily available. The revenues from different charitable waqfs started to be pooled in a common treasury. Waqf sector also played an important role in employment. During the 2nd Constitutional Period in the late Ottoman era, 8,23%; in the early Republic years 12,68% and in 1990's 0,76% of the total work force was employed in the waqf sector (Öztürk, 1995).

Nevertheless, the centralization process was followed by a decentralization move until the nineteenth century, while the ever-lasting effects of the centralization acts and codes were observed in the nineteenth and twentieth centuries (Çizakça, 2000). The centralization (and to some extent nationalization) of the waqf system can be read as a significant step towards Westernization of the society. The great powers of the time, namely England, France, and Germany, were all demanding the abolishment of the waqf-system following the Crimean War (Çizakça, 2000). The pro-Westerners tended to view all traditional institutions as responsible for economic and political descent. European policy makers also contributed to such a transformation in the waqf system since centralization would allow the governments to hold much more control over their societies. The

Europeans thought stronger states would find it easier to pursue Westernization (Kuran, 2001). The corruptive tendencies among the system exaggerated the worsening situation despite some diligent and sincere attempts to get the waqfs recovered.

The transition in the waqf system did not happen easily since in most of the modern Middle Eastern or Islamic states, governments made many confiscations/expropriations of vast waqf property which were religiously considered as sacred. On the other hand, the centralization processes in the Muslim world has increased the monitoring and management costs since the foundation of *Nezaret* in the late 19th century of the Ottoman Empire. The waqfs had to finance their own operations and additionally, the expenses of the state bureaucrats that are presumably responsible for monitoring the waqfs' operations. This occurred while the bureaucracy's misuse of the monitoring power led several cases of indirect confiscation of waqf revenue or property through faulty annual reports that were subject to tax-exemptions (see Çizakça, 2000).

The modern waqf system (in most countries under the secular law) continues to keep its fundamental foundations, such as sacredness of the founders' will and the type of the property. Modern waqf is a corporation, an internally autonomous organization that the courts treat as a legal person. Mostly a board of mutawalli manages the modern waqfs, instead of an individual. The legal infrastructure is modified to give wider operational powers to the mutawalli boards (Kuran, 2001). This does not mean the mutawallis are unconstrained by the founder's directives, however. Waqfs can participate in businesses within the limits of the endowment deed and their operations are under legal monitoring. They are allowed to operate with pooled resources which assumingly would create economies of scale. Their founders may include the government, other non-governmental institutions, or firms. Their assets can be in many forms, including cash and stocks (Kuran, 2001). Mutawallis enjoy greater flexibility in waqf operations, management, disbursement, and investment decisions. Waqfs are still useful instruments for providing or, in many areas, complementing social services such as financing mosques, schools, hospitals, libraries, and monuments, but they are not seen as the primary suppliers of public goods. In most of the Middle Eastern and other Islamic countries, governments have become the primary providers of public goods. The much more effective enforcement of property rights today, as compared to the past, is argued to reduce the waqf system's importance as the most plausible vehicle for wealth sheltering. As a general conclusion on the current position of the waqfs, the secularization process during late Ottoman and early Turkish republic periods led the waqf

system to lose its religious motives as well. They were regarded mostly as inefficient economic structures with vast resources. Therefore, during 1920-1949 and 1960-1970, large confiscations and sales of the waqf property were observed in Turkey.

The waqf system has been neglected and almost became extinct since the early days of the modern Turkish state until the 1967 act that reconstituted the legal conditions of awqaf in the Turkish law. It is recorded that merely 73 new waqfs were established between 1923 and 1967 while this number is calculated to be more than 4000 since 1967, quoted Çizakça (2000). Since then, the waqf system has been revitalized, though still under state monitoring and control. The number, size (in terms of revenue), and scope of awqaf flourished dramatically through the 1980s and 1990s, despite several attempts to limit the waqf system's potential. Today, Turkey enjoys the existence of waqf institutions either founded by secular or religious motives. As of 1987, there were approximately 37,917 properties of awqaf in Turkey (Çizakça, 2000). Moreover, the waqf system in Turkey has always played a significant role of providing employment opportunities as it counted for 8.23%, 12.68% and 0.76% of the total employment figures by 1900, 1931 and 1990, respectively (Çizakça, 2000).

4.2. An Institutional Approach to the Waqf System

Besides functional market institutions, the very demand for a non-market institution in the Islamic history is also a strong motive for the creation of such philanthropic institutions throughout history (Çizakça, 2000). As stated in above sections, there are many similarities to the philanthropic institutions, *trusts*, in the West, despite the arguments that the Western institutions turned out to be more flexible compared to the waqfs (Çizakça, 2000). According to one definition, awqaf are described as “redistributive institutions and poor relief agents” while not being special ventures for profit maximization or for establishing large corporations (Orbay, 2006), quoted Esmaili (2010). Convincingly, waqfs are argued to solve the issue of under provision of public goods as they mainly offer such services that are often considered as public, of course, resultantly, non-rival and non-excludable (Çizakça, 2000).

Institutional perspective on the evolution of awqaf and its current administration throughout the Islamic world is often assessed on the grounds of property rights. This is due to the excessive number of public goods providing awqaf in the history of Islam. Therefore a vast neoclassical

literature on the agency problem and its extensions such as shirking, misalignment of interests, monitoring costs are easily applied to an institution (waqf) which differs from traditional Western trusts in many ways. North (1990) however emphasizes the importance of ideology in creating institutional change. He argues the existing institutions, both formal and informal, provide an incentive structure within which economic, political, and social organizations develop. His argument is partly inherited by Acemoglu et al. (2005) as they argue the current institutional base in a country will have a profound impact on the next period's institutional construction. However, North (1990) adds the ideological perspectives as a factor that affects the pace and direction of institutional change while further arguing some of the European countries lagged behind due to such ideological differences. He also cites the informal institutions, the role of property rights, and the role of organizations as important elements of institutional change.

The issue of secure property rights, for instance, is said to arise due to the *fatwas* of the Islamic courts, involvement of Islamic inheritance law, and the potential agency problems, according to Shatzmiller (2001). Different juristic approaches to the issue of transferring property rights in the main schools of Islamic thought is considered as another obstacle on ensuring property rights over the endowments, Shatzmiller (2001) argues. More emphasized are the cases where the property rights (i.e. for the lands subject to endowments) are shared among two or more owners. Providing examples of the *free rider* problem from the 12th and 15th century Fez, Shatzmiller (2001) concludes the institutional history of the *public good waqf* was distinct from that of the *family waqf*. The charity foundations that provided public goods or services faced multi-faceted challenges in their operations compared to the family endowments, she asserts. The strictly legal and economic aspects of the public good waqfs increased the management costs considerably while leaving rooms for conflicting interests and potential agency problems. In that regard, Shatzmiller (2001) provides instances of fatwas which show institutional behavior resulting in loss of revenue, confusion, interruption of work, increased costs, declining revenue, or no income at all. Once Islamic societies enjoyed over-supplied public goods and services via well-functioning waqfs, centralized government sector was nearly non-existent for centuries. Following the economic and political decline of the Islamic states however, waqfs –especially the ones providing public goods- suffered hugely.

However, the waqf system should be assessed under a multi-dimensional approach, including the Islamic culture, law, and other secular means (i.e.

economy), in order to reach a comprehensive institutional understanding. Islamic elements mostly represented by the divine law and cultural inheritance are often cited as the inhibitive factors that led the Middle Eastern and Islamic countries to economic stagnation for centuries. According to Kuran (2004), for instance, Islamic contract law and inheritance law are among the leading factors along with the waqf system that caused underdeveloped economies throughout the Islamic world. The issue of private property is also analyzed by Messick (2003: 723) with special reference to the case of Yemen, as he considers the judicial problems which arose after the application of Islamic inheritance law and cites the resulting issues from the exercise of preemption rights following the sale of an inherited land share by one of the shareholders to a third party. On the other hand, Kuran (2007) argued the perpetuity principle in the foundation of waqf led to the properties owned by the waqf becoming unproductive and inflexible. However, in Coasian terms, the initial delimitation of legal rights established by the legal system has importance on lowering contractual and transaction costs, while the type of contracts made is important because long-term contracts have lower costs. Coase (1960) made his point on the property rights argument on the basis of the efficient allocation problem and the inefficiency arising with government regulation in any industry. Likewise, one might argue, contrarily to the arguments against the own-decay of the waqf system, the state intervention into in the late Ottoman period made the case even worse and more costly to manage. Therefore, the only inflexibility under the perpetuity principle is the non-transferability of rights which in some cases were re-defined over changing circumstances.

According to Kuran (2011), what made the Middle East fall behind the West in terms of economic performance is not the conservatism or hostility towards commerce; rather, it was the lack of proper institutional base that was mostly represented by traditional ones that failed to generate incentives for organizational innovation in the private economy (Kuran, 2011: 10-11). The arguments by North (1990) or Acemoglu et al. (2005) suggesting the Western traditional institutions by-force or organically evolved into new ones through the rapid changes in social and economic structures might be read as supportive to the ideas brought forward by Kuran (2011). It is, however, more interesting to observe that many Middle Eastern nations faced with economic decline throughout the 19th and 20th centuries. They are very likely to have witnessed the abolishment of traditional Islamic institutions and insertion of the modern Western ones. Kuran (2011) brings his arguments forward as he asserts the differences between inheritance

practices in the two regions (Mideast and West) had enormous implications for institutional development through time, while also arguing the waqf institutions led to the blockage for the development of self-governing organizations outside the state which is essential to a strong civil society (Kuran, 2011: 11).

Following Kuran (2001), Esmaeili (2010) underlines the differences between the legal nature of the waqf institution and land ownership system in the Islamic law and the trust institution and real property law in Western countries. He argues that such differences are relevant in understanding the Muslim nations' failure to establish a rule of law system. On the contrary, Çizakça (2007) argues the traditional institutions stemming from Al-Ghazali's (economic) principle of *maqasid al-shari'ah* (i.e. *awqaf*), which have been inspiring to the Western states, are compatible with the current successful modern economies' institutional and governance structures in their basics (Çizakça, 2007).

Schoenblum (1999) also argues the waqf, as compared to the trust in Western tradition, could not cope with the changing environment, while the trust law has effectively and formally responded to meet changed circumstances (Schoenblum, 1999). In contrast to the waqf, the trust, from the time of its origins as a use, has been the epitome of a vaguely defined legal construct able to address practical wealth management and disposition requirements of property owners, according to Schoenblum (1999). With that regard, it is worth noting that an argument against the negative perception of the legal nature of family waqfs, the far less common practiced form of *awqaf* in the history of Islam [Quoted in Çizakça (2000): According to the figures provided by Barkan, the family/charity waqf ratio in the 18th century was 14.20% and 16.87% in the 19th century, in terms of total revenue], are mostly founded to protect the family's wealth and prosperity from arbitrary confiscations of the rulers, according to Köprülü (1942) and Gerber (1988: 35), quoted by Çizakça (2000: 24).

Kuran (2004 and 2007) seems to have fallen to the same mistake of using the governance indicators and institutional basis in a country interchangeably. Although there is no clear distinction between the two in a vast body of literature, it is quite evident that the governance indicators, as well as policy choices, are the result of long-run evolving institutions. Hence, Islamic law, or *shari'ah*, has not prohibited nor inhibited economic activity while its poor practice in many areas, including the waqf system, led to economic inefficiency and poor redistribution of wealth among the societies. When the Ottomans are particularly considered, the unfavorable

economic policies pursued by the government, and thus an insecure environment for capital accumulation for centuries led to small firm sizes. On the other hand, geographical disparities, controls over prices (*narh*) and profits, high interest rates due to deteriorating economy, property rights restrictions and wide-spread confiscations created instable economic agents (Çizakça, 2010). It is convincing that the unfavorable conditions for the well-defined and secure property rights to flourish in the Ottoman Empire left the once well-functioning waqf system intact and caused its decline. The relative flexibility in court decisions, on the other hand, was misused and often caused moral hazard issues. Therefore, it is neither the rigidity of shari'ah nor the Islamic inheritance or contract laws that led to economic decline in the Islamic countries, as implied by Kuran (2011), which are mostly characterized by the waqf system. It seems that excessive governmental intervention and the principle-agent problems that impeded the establishment of well-defined property rights in the Islamic world are to blame for the current underdevelopment.

Lastly, Mohammad and Mar Iman (2006) propose an alternative thinking of the perpetuity principle of a waqf through their distinction between the perpetuity of a physical object and its 'dedication' of benefits. Their contribution is the attachment of a value to the physical property (immovable) and its non-transferability as they offer any valid valuable thing as the medium of waqf such as cash, equities, goods and services which be treated same as land and other immovable properties (Mohammad and Mar Iman, 2006). No matter what measures are taken to revive the waqf system in the modern economies of the Islamic world, it is crystal clear that such charitable endowments should be complementary to the governments' economic functions. Thus, we may sum up with the following argument from the Turkish case that both the country's overall economic and political environment, as well as the condition of its waqf sector could improve though the private entities' entrepreneurship is expected to further develop. This is followed by the increasing number of endowments to reinstate social justice and other means complementary to economic success.

In this regard, we will conclude this section with a short emphasis on Turkey's experience with the rise and decline of awqaf in parallel to the changes in its institutional structure, which is measured through several distinct governance indicators. In order to understand the relative dynamics of the waqfs' development to that of Turkey's overall governance performance, relevant descriptive statistics of the last three decades are presented in the appendix. The figure and tables all indicate a parallel

improvement in both Turkey's economic and governance performance and the waqf system in terms of the newly established endowments over the period of 1980-2010. Therefore, our previous argument on the social and economic role of waqf institution that is described as being complementary, rather than substitute, to government institutions seems to be justified with the data from Turkey's recent experience. The arguments that relate poor management issues on the micro-scale with macro-perspective generalizations about the institutional base in the Islamic world fail to describe the real motives of founding awqaf and reasons of their historical rises and declines. Lastly, our data from Turkey and the discussions around waqfs' historical trajectory suggest charitable organizations or Islamic waqfs, in specific, do not emerge due to the lack of well-defined property rights and the rule of law in a society while they flourish under such an environment that leans on sound institutional basis.

5. Conclusion

This brief overview and analysis of the waqf system in the Islamic world, emphasizing Turkish societal tradition, implies that even in undemocratic and non-western social organizations, definition and protection of property rights could be regarded as fundamental issues in formation of a social organism. Waqfs have been seen both philanthropic and economic institutions which made them an important socio-economic actor for centuries. The most important aspect of this system is the provision of public and private goods. Although it can hardly claim that these institutions represent a modern type of institution with fully defined property rights supported by law, they provided some basis of protection of wealth and a pragmatic solution to the structural and financial problems regarding the public goods/ services. The Islamic community has preserved a long-lasting tradition of these institutions that still have impacts on shaping the societies.

Special attention to the structure of the system in the Ottoman State was given because of the extent that waqf institution reached its peak level in both organizational and operational dimensions. Today, the waqf system can be modified and supported as an important economic partner to the business sector in both operational and financial senses. On the other hand, charitable waqfs can be regenerated in most of the local areas to provide public goods which turn out to be in service forms today.

The inefficiencies stemming from the foundational aspects and operational rigidities can be reassessed and reduced with appropriate adjustments. Regarding the Turkish case, the heavily government regulation

should be removed and waqfs should be given more legal and bureaucratic freedom. Counting the Waqfs Bank of Turkey first, many waqf foundations and property are still managed and/or controlled by the State. The government is suggested to remain outside of the system, allowing the waqfs to operate in a decentralized way. Given a more sound legal basis and better defined property rights in Turkey, the waqf system can operate more efficiently. Supported by the arguments put forward by Çizakça (2000), the rebirth of the waqf system is essential, given more room for operation under flexible laws and governance structures, beginning with the abandonment of the modern hostility towards such institutions and paving the way for a comprehensive reform (Çizakça, 2000). Last but not the least; awqaf could function as complementary structures for policy reforms in the economic scheme while creating the suitable basis for institutional diversity for economic freedom and democratization of the modern Islamic societies. Opening more space to the waqf system parallel to other governance structures will only enhance social capabilities and increase the role of individual contribution to the economic activities through non-governmental means.

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Appendix

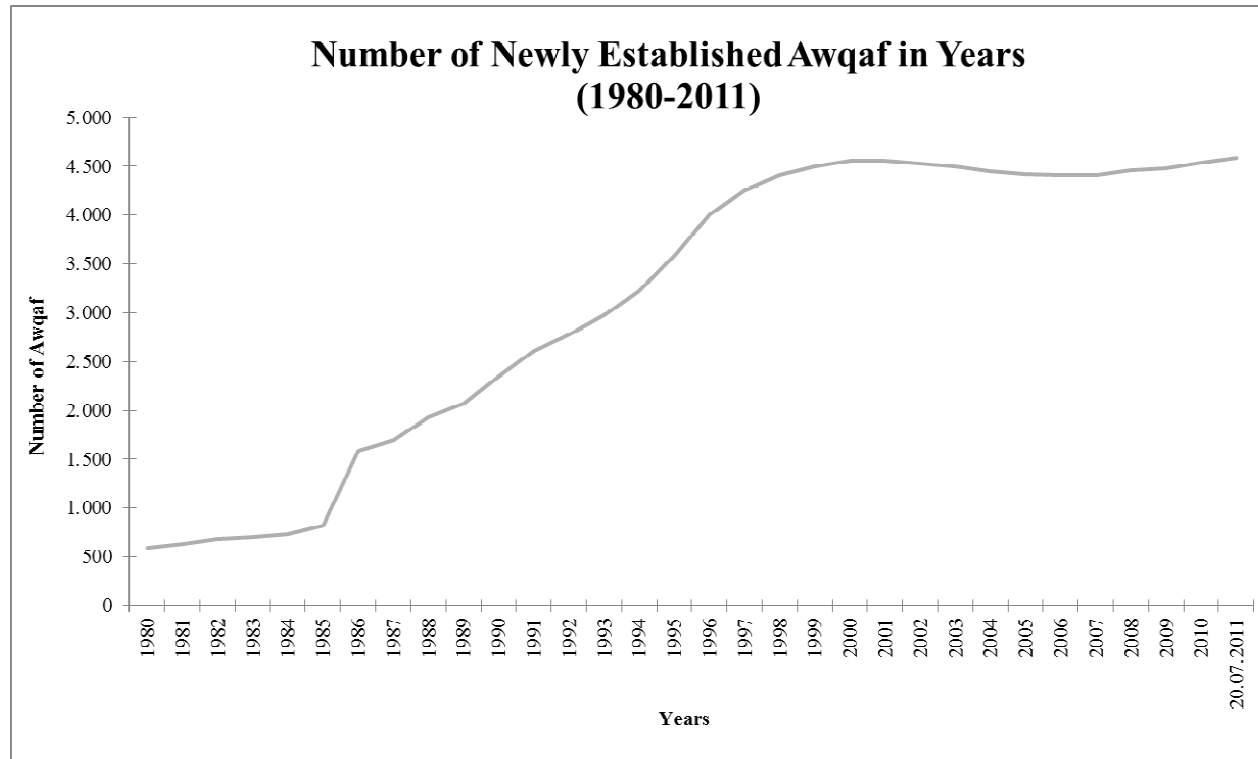


Figure 1. Number of Newly Established Waqf in Turkey (1980-2011), Directorate General of Foundations

The following information on the structure and sources of International Country Risk Guide's (ICRG) Political Risk Services' data provides a useful overview to the governance indicators used in this study:

“The aim of the political risk rating is to provide a means of assessing the political stability of the countries covered by ICRG on a comparable basis. This is done by assigning risk points to a preset group of factors, termed political risk components. The minimum number of points that can be assigned to each component is zero, while the maximum number of points depends on the fixed weight that component is given in the overall political risk assessment. In every case the lower the risk point total, the higher the risk, and the higher the risk point total the lower the risk. To ensure consistency, both between countries and over time, points are assigned by ICRG editors on the basis of a series of pre-set questions for each risk component.” (ICRG, 2011)

Component	Points (max.)
Government Stability	12
Socioeconomic Conditions	12
Investment Profile	12
Internal Conflict	12
External Conflict	12
Corruption	6
Military in Politics	6
Religious Tensions	6
Law and Order	6
Ethnic Tensions	6
Democratic Accountability	6
Bureaucracy Quality	4
Total	100

Indicator	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	
Bureaucracy Quality	2	2	2	2	2	2	2	2	3	3	3	3	3	2,583	2	2	2	2	2	2	2	2	2	2	2	2	2	2
Democratic Accountability	3,833	4	4,25	5	5	4,417	3,75	4,333	6	6	6	4,833	5	3,583	2	3,583	4	3	2	3,75	5,375	5,5	2	2	2	2	2	
Ethnic Tensions	2	2	2	2	2	2	2	3	3,417	3,25	2,5	2	2	2	2	2	2	2	2	2	2,042	2,5	5	5	5	5	5	
Law and Order	3	3	3	3	3	2,75	2	2,083	4,167	4	4	4,5	4,417	4	4	3,333	3,917	4	4	4,208	4,5	4,5	5	5	5	5	5	
Religious Tensions	3	2	2	2	2	4	4	4	3	4	4	5	5	5	5	5	5	5	5,5	5,5	5,5	5,5	5,5	5	5	5	5	
Military in Politics	3	3	3	3	4	4	4	4	5	5	4,5	3,333	3	2	1	1	2	3	2,917	2,917	4	4	4	4	4	4	4	
Corruption	3	3	3	3	3	2,083	2	2,417	4	4	4	3,667	2	2	2	2	2,583	2,833	2	2,333	2,5	2,5	2	2	2	2	2	
Ext Conflict	8	8	8	8	7,5	8,417	8,25	8,75	10	10,33	10,83	9,5	9,083	9,583	8,25	9,25	9,5	8,542	10,42	8,625	8,625	9,25	11,5	11	11	11	11	
Internal Conflict	6,833	7	7,083	7	6,333	6	5,917	6,167	7,667	8,167	7,5	7,25	7,417	7	4,25	4,25	7,667	8,375	9,333	9,417	9,042	9,583	10,5	10,5	10,5	10,5	10,5	
Investment Profile	8	6,583	6,167	6	5	4,25	4	4,167	5,917	6	5,083	5	4,75	7,083	8	8	9,75	7,708	7,833	7,5	7,875	8	8	8,5	8,5	8,5	8,5	
Socioeconomic Conditions	7,417	7	6,75	6	3,75	2,417	2,083	3,917	6,5	5,333	5,917	5,75	4,5	2	2	2,417	2	3,333	4,25	5	6,375	6,5	6,5	6,5	6,5	6	6	
Government Stability	8	7,75	7	6,333	5,583	3,667	4,5	5,417	8	6,333	5,083	5,5	6,833	9,083	10,08	9,75	9,667	7,625	7,042	9,5	9,625	10	11	11	11	11	11	

Table 1. International Country Risk Guide (ICRG) Indicators, Turkey (1984-2010)

Economics of Philanthropic Institutions, Regulation and Governance
in Turkey

The below data in Table 2 shows different governance indicators created by the Fraser Institute and the Economic Freedom of the World (EFW) Report. The first column refers to the government's share in the total GDP of Turkey in years; the second column is the index constructed by the *Global Competitiveness Report* surveys as well as the ICRG data. The third and fourth columns are constructed by *Global Competitiveness Report* surveys along with the World Bank's *Doing Business* data. The fifth and sixth columns refer to Turkey's ranking in terms of 5 broad categories through years. For the second, third, fourth and fifth columns, the higher the index is the better for economic freedom.

Years	Size of Government	Legal System & Property Rights-- Adjusted	Time with government bureaucracy	Regulation-- Adjusted	Rank	Percentile
1980	4,4	5,6	-	4,4	99	5%
1985	4,9	5,8	-	5,2	81	27%
1990	5,8	4,5	-	5,1	88	22%
1995	6,9	4,8	6,2	6,1	76	39%
2000	7,1	5,4	5,2	5,6	96	20%
2001	6,7	4,1	6,5	4,9	109	11%
2002	7,0	4,5	5,3	5,2	109	11%
2003	7,5	5,3	5,3	5,4	95	25%
2004	8,3	5,2	4,8	5,1	85	33%
2005	7,8	6,5	6,2	5,6	97	31%
2006	7,4	6,3	4,3	6,0	91	35%
2007	7,5	5,7	4,8	6,1	92	35%
2008	7,4	5,6	5,1	6,0	74	48%

Table 2. Fraser Institute EFW Data, Turkey (1980-2008)