Sukuk-waqf: The Islamic Solution for Public Finance Deficits

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Abstract-- The majority of Muslim countries face increasing pressure on their budget, which pushes to more public spending. Eventually, the main victim of this situation will be the welfare of Muslim communities. Despite Islam does not tolerate negligence regarding the importance of State as major player in preserving the welfare of Muslim communities, it offers a third option to support public effort through the institution of Waqf. Indeed, this institution has played a crucial role all along Muslim civilization and it is invited to more innovation to answer to today’s challenges. Sukuk-Waqf can be seen as the perfect sustainable financing instrument offered by Islam to help sustain public spending by the people and for the people. This paper will try to examine the concept of Waqf, cash Waqf and Sukuk Waqf in Islam and their evolution during Muslim civilization. Finally, it will go through modern attempts to implement this model that can answer the need for financing to support public effort to preserve the welfare of Muslim citizens.

Key words: Sukuk-waqf, public spending, sustainability.

I. INTRODUCTION

Upon this earth, wealth belongs to Allah as He is the sole Creator of everything. However, Humans were chosen to accomplish the duty of viceroyalty on this earth by exploiting the bounties given to them through economic activities permitted by Islam. Consequently, Humans acquire and transfer properties through different form of contract that can be divided into lucrative and non-profit transaction. Waqf can be categorized under the second type of contract of non-profit transaction. It be defined as the concept of dedicating any property for posterity from which its profit may be used for any charitable intention [3].

Prophet Muhammad once said: "The record [Book of Deeds] is closed when a person passes away, yet those who leave behind knowledge, good children or works of charity are exceptions. Good deeds will continue to be written in that person's record.”

Prophet Muhammad founded Waqf himself and advised his devotees and future Muslims followed his advice. He donated the date garden in Khayber to Muslims.

Waqf-like charity has a history older than Islam, which seems to have existed in ancient Mesopotamia, Greece, Rome as well as pre-Islamic Arab Societies [7]; [15]; [18]. Lately, all empires that ruled on Muslim territories have given a crucial place to Waqf institution as a tool to develop and secure the welfare of Muslim communities. Indeed, throughout History, Muslim civilizations have adopted the concept of Waqf mainly to mitigate the burden of public services especially during the Ottoman Empire where the size of Muslim population reached more than twelve million and a half Muslim [13]. One can say that no such thing as municipal authorities had ever existed in those cities, the Waqf proved the most important (if not the only) means by which Ottoman sultans and senior state officials could provide their citizens with the most basic and essential public services [14]. Moreover, Waqf has been promoted to a viable pillar of state governing as it considerably helps rulers to optimally govern with a high level of financial ease. Even government financing of education used to take form of constructing a school and assigning certain Waqf property that provides regular revenues to cover operating expenses of the school [6].

The current economic situation of almost all Muslim countries in terms of their illiteracy rate, lack of good healthcare, high unemployment rate, and the spread of poverty is a call to policy makers and researchers to rethink strategies to re-born Waqf institution. Furthermore, the need for growing infrastructure project is a crucial component of the growth equation for any country. However, states
cannot afford taking big investment project alone anymore due to budget constraints, global recovery slow down and the fallen of raw materials prices. In fact, basic social needs should maintain a parallel growth similar to the demographic growth as to satisfy the population’s demand but the lack of financial resources breaches this rule leaving the way to disequilibrium within the society that can put the stability of states in jeopardy. Consequently, public sector and government should search for sufficient sources of financing and private sector sounds to be the optimal fit for this equation. Nevertheless, Muslim communities have another way that might solve the problematic of infrastructure financing which is the development of Sukuk-Waqf as an efficient instrument to secure sustainable financing for the growing needs for infrastructure. The adoption of such instruments aims to combine both religious duty of charitable spending and economic development.

This paper aims to raise the attention of public to the crucial role of Waqf to solve the current lack of financing towards infrastructure projects that impedes the development of Muslim countries. The proposed instrument is composed of two Islamic products, which are Sukuk and Waqf. Both of them will help to make the idea of Waqf within reach of all Muslim in order to make economic development a matter of all the community.

II. THEORETICAL FRAMEWORK OF WAQF

In the Arabic language, the word “waqf” (pl. awqaf) literally means to hold, confine, prohibit, detain, prevent, or restrain. Legally, it means “to protect something, by preventing it from becoming the property of a third person” [11]. In other terms, Waqf is an endowment made by the rich to benefit the poor. It is one of the important elements in Islam in alleviating poverty through providing basic needs to increase general welfare of people [19]. In Islamic Law, Waqf requires restriction of a particular property as it is highlighted from the literal definition despite the existence of some divergences regarding the periodicity of Waqf. The Hanafis, Chafi’is and Hanbalis opt for a permanent Waqf. However, it could be temporary for the Malikis who confirm that the Waqf has the right to define a certain period for the contract, which by its end the property returns to him. In other terms, Waqf is also explained as an action of conserving some property for a specific charity that prohibits any use of it outside the specific purpose [5]. Property/money provided as Waqf ceases to belong to the contributing individual or organization. Waqf cannot be transferred to anyone, inherited or put up for sale, since it is considered to belong to Allah (SWT) [10].

The structure of Waqf is based on four elements: the Waqif, the element endowed (Mawquf), the beneficiary (Mawqif ‘alayh) and the form of the contract (Al-sighah). For each element cited below, there is certain condition by which the process of Waqf is considered valid.

According to ElKhatib (2016) the waqif or founder of the waqf must be a:

- ‘aqil: (someone in full possession of their mental capacity)
- Baligh (adult)
- Hurr (free person)
- Capable of transferring the ownership of the asset or property from himself to the ownership of Allah

According to Mahmood (2008), the corpus must be entirely owned by the donor before he/she contributes it and he/she understands that his/her has to relinquish responsibility of the assets since ownership is transferred to Allah (SWT). Once the element endowed is given to the waqf, the role of the donor toward his/her assets becomes inactive, and a manager or trustee of the Waqf property will take over responsibility to utilize the property in line with the donor intentions [4].

The founder should specify the beneficiaries in his will or waqf deed. They should be members of the family of the founder or members of public who are in need for financial assistance. The Benefit of the trust can also be allocated to activities such as building a medical facility, mosque, or setting up a shelter or a school [8].

The contract is normally prepared in writing (orally declaration is also allowed), to avoid disagreements or misunderstandings in the future and also for record purposes [4]. An example of Al-sighah normally employed is “I donate my land as a waqf for the sake of helping needy”.

Originally, the periodicity of Waqf is to be eternal according the Hanafis, Hanbalis and Shafii’s. However, the Malikis authorize a Waqf restriction of one year or so for a known period to which after its achievement, the ownership returns to the Waqf or other.

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2 Islamic Schools of thought are in the number of four: Malik, Shafi’i, Hanbali and Hanafi.
3 Al-charh al-saghir li-dardir 4/94
4 The forms by which Waqf contract is been established.
5 Bada’i’ Al-sana’i’ lil-kassani 336/6.
From *Maqasid Al-shari’ah* perspective, cheikh Tayyeb ibn Achour listed four roles of *Waqf* in Islam:

1. Encouraging and multiplying *Waqf* actions as it brings public and private interest (*Maslahah*). For that, it is recognized by shari’ah as deeds which Divine reward is continuous after one’s death. The Messenger of Allah peace be upon Him said, “When a man dies, his deeds come to an end except for three things: *Sadaqah Jariyah* (ceaseless charity); a knowledge which is beneficial, or a virtuous descendant who prays for him (for the deceased).”

2. For the *Waqf* to be given from a clear and unhesitating conscious because it is consider as a *Ma’rouf* and a generous act. Also, *Waqf* is given with no expectation of an instant compensation. Therefore, the highest intention of *Waqif* is public good and Allah’s reward.

3. Offering and providing a multitude of means by which *Waqf* can be achieved. This objective fully falls into the first one of inciting and encouraging *Waqf* actions.

4. Not making *Waqf* an excuse to waste the money of heirs or debtors as it was the case during the time of *jahiliyya*.

It is obvious that *waqf* represents the highest form of giving in Islam because of its privileged value and the sustainability that it presents. It can be seen as a genius response of Islam to public financing through unconventional ways. Indeed, as most of countries suffer budget cuts and the pressure of public debts, *Waqf* can be the perfect instrument to rebalance the equation and preserve the welfare of Muslim communities.

III. CASH-WAQF

The cash *waqf* is a form of certificates with different denominations to raise money against the planned projects. The issued certificate will be bought by a number of individuals or institution to finance the planned projects. Separate cash *waqf* will be raised for each individual *waqf* activity [12]. Historically speaking, Çizakça (1998) stated in his paper that during Ottoman economy, cash *waqf* played important role.

According to classical Scholars of *Hanbalis* and *Shafi’is* cash *Waqf* is not permissible, because cash *waqf* results of consuming the money in order to spend it. Because of that, the element endowed in this case money is destroyed by the act of spending10. Oppositely, the *Malikis* and *Hanbalis* consider cash *waqf* permissible. *Ibn Taimiyyah* quoted from *Ahmad bin Hanbal* and said that cash *waqf* is beneficial through utilizing it.

In its fifteenth meeting, *Al-mujamma al-fiqhi* (Islamic Fiqh Academy) issued a statement N°140 that confirms the permissibility of cash *Waqf* ending the discussion of this issue.

Based on *Maqasid Al-shari’ah* cited in the previous section, Ahmed Hadad the Grand Mufti of Dubai11 extended these *Maqasid* to cash *Waqf*. They can be resumed as follow:

1. The implementation of cash *Waqf* will, evidently, encourage more individuals to restrict part of their wealth, as contribution would take form of small amount of money, which will amplify the practice of *Waqf*.

2. As for the matter of clear and willing conscious, cash *Waqq* through small or big amount is obvious evidence that the *Waqf* does not ask for anything else except the blessing of Allah.

3. The expansion of cash *Waqf* falls logically in the *Maqsid* of diversifying the means by which *Waqf* is practiced and offers an alternative to those with small means.

4. The *Maqsid* of not wasting others wealth exists in cash *Waqf* because of the structure of such instruments that accepts all amount of contribution, which cannot cause any harm for anyone’s wealth or heritage.

The current structure of cash *Waqf* can be presented as follow:

Figure I. The General Structure of Cash-waqf Operation

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10 See Al-mughni by Ibn-Kudama 5/640
The presented structure offers a high level of flexibility regarding the use of the proceeds depending on the need of community. Although the Waqif specifies the use of its money within the contract, the structure can be personalize to match the needs of the community though different pools.

Additionally, cash waqf is a special type of endowment that differs from the ordinary real estate waqf in that its original capital consists, purely or partially, of cash. Social Islamic Bank in Bangladesh has been offering a cash waqf deposit for a few years now. Other banks offering deposits based on the cash waqf include Islamic Bank Bangladesh, EXIM Bank, Bank Asia, Shahjalal Islami Bank, Al-Arafah Islami Bank, Prime Bank (all in Bangladesh) and Bank Islam in Malaysia. All these are examples of indirect cash waqf models.

IV. SUKUK-WAQF

The origins of sukuk can be traced back to the classical Islamic period (700-1300AD) where a sakk (singular of sukuk) was used to describe any document representing financial liability. This instrument represents financial obligations resulting from trade and other commercial activities. Such practice was practiced in conformity with verse 2:282 of the Holy Qur’an:

“When ye deal with each other, in transactions involving future obligations in a fixed period of time, reduce them to writing…It is more just in the sight of God, more suitable as evidence and more convenient to prevent doubts among yourselves.”

The International Islamic Fiqh Academy issued a statement in 1988, holding that “Any combination of assets (or the usufruct of such assets) can be represented in the form of written financial instruments which can be sold at a market price provided that the composition of the groups of assets represented by the sukuk consist of a majority of tangible assets”.

According to AAOIFI, Sukuk is defined as: “Investment sukuk are certificates of equal value representing undivided shares in ownership of tangible assets, usufructs and services or (in the ownership of) the assets of particular projects or special investment activity, however, this is true after receipt of the value of the sukuk, the closing of subscription and the employment of funds received for the purpose for which the sukuk were issued.”

The securitization of assets is a highly important stage for the development of capital raising because of its standardization and regulation. All strategies that aims to raise sufficient funds through public source shall opt for Bond or Sukuk in the case of Islamic finance.

Sukuk-waqf is composed of a merger of Sukuk based contract and Waqf. It can be defined as tradable certificate of equal monetary value that represent the money restricted (Al-mal al-mawqaf) [17].

There is a variety of types of Sukuk, which are based on the existing Islamic contracts: Murabahah, Ijarah, Mudarabah, Musharakah, Wakalah and Salam. Other hybrid and complex structure of Sukuk can be found depending on the development of Islamic financial engineering.

The general process of Sukuk issuance which will be later used for Sukuk-waqf structuring can be presented as follow:

- Creation of an SPV to represent the investors;
- Issuance of the certificates and putting them into circulation;
- Secure the cash-flow through the period of the contract from the issuer to the investor.

Also, it is worth to note the main parties involved in the issuance of Sukuk:

- the Originator, which is the company wishing to raise funds,
- the Issuer of the Sukuk, which will be an existing or a newly incorporated special purpose vehicle (“SPV”);
- the Lead Arranger/Manager, which is the party arranging/managing the whole Sukuk process;
- the Trustee, who is an appointed party to represent and oversee the rights of the Sukuk holders from the beginning of the arrangement of Sukuk issuance until the full redemption of the Sukuk by the SPV;
- the Sukuk holders, who are the investors intending to invest in the project, and who holds the Sukuk certificates as evidence of their investment in the Sukuk.

The structuring of Sukuk-waqf may not differ from the structure of investment Sukuk in the form but in the purpose. In fact, the holder of normal investment Sukuk aims at profit based on the rule of “Al-ghumnu bil ghumn”. However, the holder of Waqf-sukuk is not driven by any lucrative consideration as

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12 Global Islamic Finance Report 2015

he only aims at Allah’s blessing and serving public interest. It is important to note that it should be feasible to merge other form of financing in the case of big public project because of insufficient fund or time pressure. Al-qard al-hassan could be one the instrument that could complete the structure of the project [16].

The structure by which public authorities could raise fund for socioeconomic project can be presented as follow:

\[ K_p = a w + c ; \quad w \in \left[ 0, \frac{K_c}{a} \right] ; \quad c \geq 0 \]

With:
- \( K_p \): the total amount of the project;
- \( a \): Nominal value of Waqf certificates;
- \( w \): the slope;
- \( c \): total amount of qard al-hassan.

The other issue that may arise with the use of a debt component within the structure is the element of guaranties as the amount borrowed is due on the waqf fund. For that, it is advised to subscribe to a takaful product for more insurance and viability of the project.

The next point that requires clarification is the provenance of the funds. Normally, the most common way would be spontaneous acts from people seeking charitable activities. However, as we aim into making this instrument a sustainable support for the state in providing decent socioeconomic services to its community, effort to standardize and regulate sources of funds must be undertaken. As most of Muslim countries now have Islamic banks, the ideal path would the implication of banks in spreading the instrument of Sukuk-waqq and makes it a commonplace within their daily life. Government bodies through intensive media campaign must also engage in explaining the idea of Sukuk-waqq to their citizens and its consequences on their socioeconomic development.

Many would wonder why choosing to merge a tool of complete lucrative goals with a charitable instrument like Waqf. In fact, he market for sukuk is now maturing and there is an increasing momentum in the wake of interest from issuers and investors. sukuk have confirmed their viability as an alternative means to mobilize medium to long-term savings and investments from a huge investor base. Consequently, the chances of raising important funds through Sukuk-waqq are more likely to happen within the environment of Sukuk market.

V. WAQF AND PUBLIC BUDGET FINANCING THROUGHOUT HISTORY

A closer look into the History of our civilization will show the crucial place of Waqf within the structure of Muslim Empires. From the age of The Prophet Peace be on Him to the Ottoman Empire, Waqf played a big role in education, healthcare and defense replacing the conventional tools of public financing such as tax. One of the first example of a waqf for social purposes was a drinking water well (called Rummah), which was bought from a Jewish man to provide free drinking water to all. Although the primitive role of Waqf used to finance mosques and religious teachers, it is important to note the expansion of the financing to all forms of education from the Umayyad and Abbasside reign15. In fact, in their periods, it was fact that there were no organized structures of waqf institutions as specific departments or ministers for taking care of public works, roads, bridges, mosques, schools, libraries and hospitals in order to cover those public needs.

\[14\] Qard Al-hassan means a debt that does not generates any interest.

\[15\] Global Islamic Finance Report 2015
Zubaidah, the wife of Harun al-Rashid\textsuperscript{16}, as an individual, made land as well as cash waqfs in order to construct high ways from Baghdad to Makkah, bridges, and shelters for helpless [1].

Awqaf of the Ayubites (1171-1249) and the Mamalik (1249-1517) in Palestine, Syria, Lebanon and Egypt are good examples. Jerusalem had 64 schools at the beginning of the twentieth century all of them are Waqf and supported by Awqaf agricultural and metropolitan properties in Palestine, Turkey and Syria [6]. At its creation in 1923, three-quarters of the arable land in the Republic of Turkey belonged to awqaf. Also, one-eighth of all cultivated soil in Egypt and one-seventh of that in Iran were known to be waqf property. In the middle of the 19th century, one-half of the agricultural land in Algeria, and in 1883 one-third of that in Tunisia, was owned by Awqaf. It is surprisingly clear the remarkable value of Waqf and its stake in the economy was, which shows the leverage that it plays in creating a third option separate from the profit-based private sector and the official public sector.

The Waqf institution has reached its peak during the Ottoman Empire where Waqf is directly involved in the economic cycle through job creation, agricultural, education and public welfare. Roadhouses and arcades, bakeries, grinders, workshops of candle and lead, bozahouses, abattoirs, etc., fair and market places, which were built in order to provide religious, cultural and social institutions, generally located around a mosque, such as madrasah, library, foodhouse (imaret), guesthouse (tabhane), hospital (darussifa), bath (hamam), caravansary and residences of the officers and employee of these institutions as well as infrastructure facilities such as water channel and sewerage system with regular income (each one is to be allocated to a group of art or trade competent), comprised the skeleton of the new city or district to be built or an old city (Barkan ve Ayverdi, 1970) quoted from [20]. Also, most of our architectural masterpieces such as Suleymaniye and Selimiye were created with the help of waqfs [20]. Also, it has also been estimated that the ratio of people employed by the waqf institutions to those employed directly by the state Turkey in 1931 was 8.23% to 12.68% [1]. This shows the role of Waqf in alleviating the civilization through rapid and self-financed urbanization far from the intervention of the State.

VI. SUKUK-WAQF AND ITS MODERN APPLICATION

Questions about the viability and applicability of Sukuk-waqf should be raised by this stage. It is believed that such papers and models are always left behind after short formal discussion. However, the current awareness about the social dimension of Islamic finance has brought public attention towards Waqf again. Indeed, projects based on Sukuk-waqf have started to merge. The most important one would be the initiative of ISRA to launch a social project in New Zealand based on Sukuk-waqf. The project will be implemented conjointly by Awqaf New Zealand, ISRA and Security Commission of Malaysia. The goal is to issue the world’s first Waqf-Sukuk worth of $1bn. The proceeds of the sukuk will be utilized to establish farming industry in New Zealand and Canada. Via these farms, Qurbani (slaughtering animals) will be provided for Muslims particularly in the west. The waste of the animals and skins will be used to produce shoes and bags etc. The revenue will be used for charitable and social purposes all over the world.

Also, Indonesia has joined the path of implementing Sukuk-waqf to develop social property assets to be commercially self-sustaining.

Addition to these examples, has launched an initiative to develop and finance existing Waqf properties through Sukuk issuance. The issuance conducted by the MUIS (Majlis Ugama Islam Singapura) has raised a total of USD60 million which is significant looking at the nature of the operation. Hence, the success of this operation has led the MUIS to further extend its willingness to issue more sukuk in order to develop the existing Waqf properties in Singapore.

It is clear that this project with its worldwide dimension would provide an astonishing framework for Muslim countries to lunch the experience of Sukuk-waqf and merge it within their financing planning.

CONCLUSION

Islamic Moral Economy has provided the Umma with the adequate tools to maintain its prosperity and social development. Waqf represents the perfect illustration for this system. It played a tremendous role throughout the History of Muslim civilization. Now, it is the time that waqf should go through an innovative process in order for it to maintain its viable role within Muslim societies. Hence, sukuk-

\textsuperscript{16} Harun Al-rashid (763-809) was one of the Abbassid-era’s caliph.

http://www.ojs.unito.it/index.php/EJIF

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waqf seems to be the suitable instrument that could enhance the role of waqf and make it a common and familiar tool for Muslims who seek Divine blessing and Mercy.

As most of states struggle to match deficit limit, it becomes difficult to provide enough financing for the growing socioeconomic needs pressured by an exponential demographic decrease. Hence, sukuk-waqf seems to be the suitable remedy for public authorities to match their budget goal along with ensuring a constant prosperity for their citizens.

Sukuk-waqf can be considered as the perfect tool to mobilize fund from Muslim communities through a regular and sustainable way. It combines the flexibility of sukuk and the sustainability of waqf.

We believe that waqf could be the adequate answer for the socioeconomic problems that impede development in most Muslim countries. However, this concept would find a way to success without the engagement of both public authorities and Muslim individuals, which are aware of the current challenges that face the Umma.

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