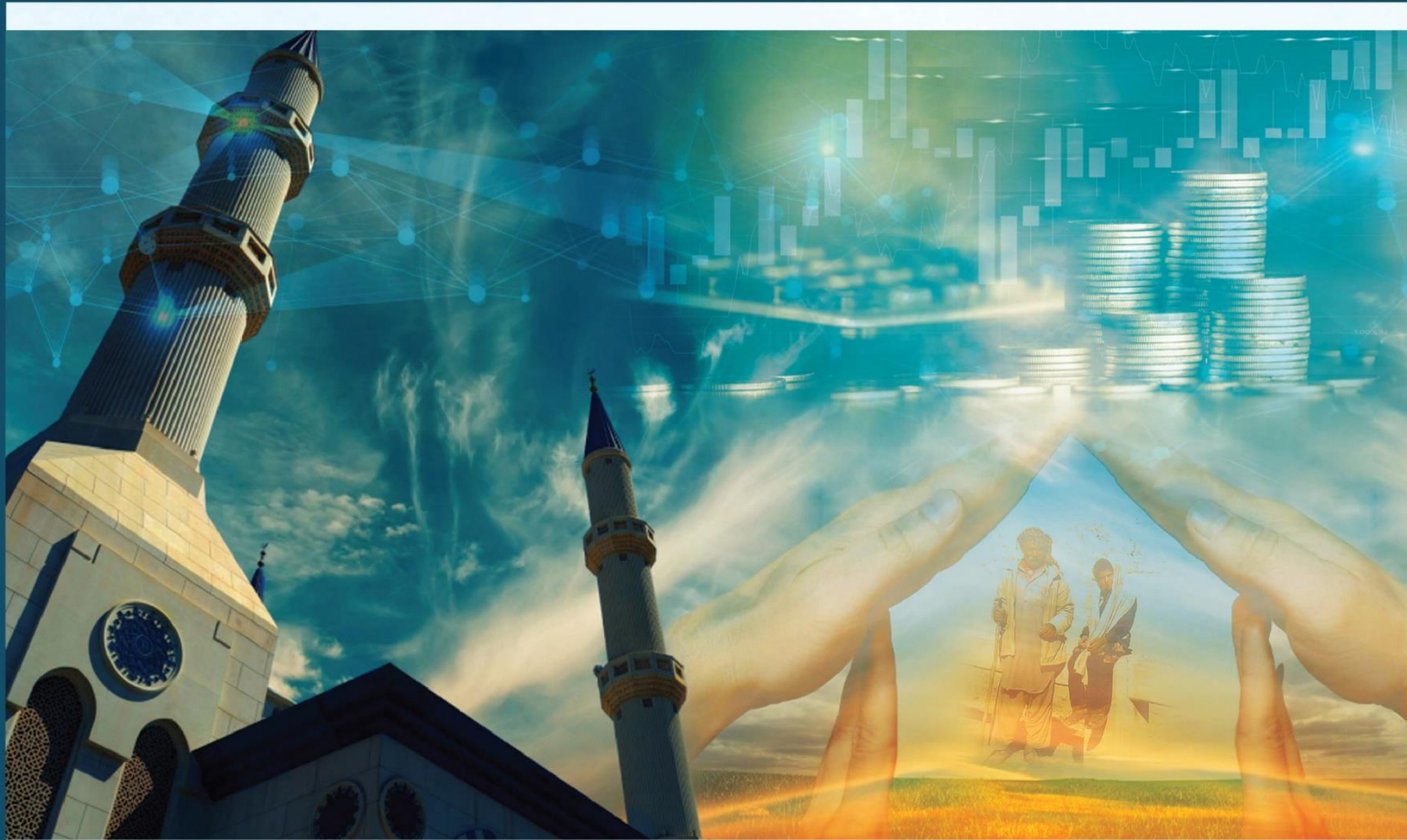
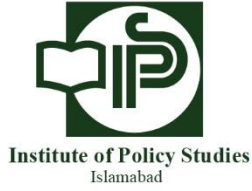


# ISLAMIC SOCIAL FINANCE FOR SOCIAL PROTECTION IN PAKISTAN



March 2023



Implemented by  
**giz** Deutsche Gesellschaft  
für Internationale  
Zusammenarbeit (GIZ) GmbH

# ISLAMIC SOCIAL FINANCE FOR SOCIAL PROTECTION IN PAKISTAN

March 2023

 [www.ips.org.pk](http://www.ips.org.pk) | [ipsurdu.com](http://ipsurdu.com)

This study has been conducted by Institute of Policy Studies, Islamabad and commissioned by GIZ under its parent project “Support to Social Protection-Social Health Protection” with special focus on two selected provinces of Pakistan (KP and Punjab).

Institute of Policy Studies, Islamabad is an independent think tank dedicated to promoting policy-oriented research, dialogue, and human and technological development for better governance.



## Islamic Social Finance for Social Protection in Pakistan

© 2023, Institute of Policy Studies, Islamabad  
March 2023

---

Dr. Salman Ahmed Shaikh  
(Principal Investigator)

Dr. Anwar Shah  
(Co-Principal Investigator)

---

For queries and feedback  
Muhammad Wali Farooqi  
Research Officer  
[wali.farooqi@ips.net.pk](mailto:wali.farooqi@ips.net.pk)

---

**Institute of Policy Studies**  
Nasr Chamber, Plot 1, MPCHS Commercial Center, E-11/3, Islamabad, Pakistan  
Tel: +92 51 8438391-3 Fax: +92 51 8438390  
Email: [info@ips.net.pk](mailto:info@ips.net.pk) URL: [www.ips.org.pk](http://www.ips.org.pk)

## Contents

Acknowledgements.....	9
Message from GIZ.....	11
Executive Summary.....	13
Foreword.....	16
Chapter 1.....	18
Social Protection and the Islamic Welfare Approach.....	18
1.1. An Introduction to the Islamic Welfare Approach.....	18
1.1.1. Distribution of Wealth.....	19
1.1.2. Principle of Self-Reliance.....	19
1.2. Zakat – The Fundamental Social Protection System in Islam.....	20
1.2.1. Importance of Organized System for Collection and Distribution of Zakat.....	22
1.3. The Context of Pakistan.....	22
1.4. Need for Social Protection in Pakistan.....	24
1.5. Introduction to the Study.....	26
1.5.1. Study Objectives.....	27
1.5.2. Study Questions.....	28
1.5.3. Research Design and Methodology.....	28
1.5.4. Data Collection Methods.....	30
1.5.5. Methods of Data Analysis.....	31
Chapter 2.....	32
Introduction to Islamic Social Finance in Pakistan.....	32
2.1. Market-Based Islamic Social Finance Institutions.....	32
2.1.1. Takaful: Concept and Structures.....	32
2.1.1.1. Takaful Products.....	33
2.1.1.2. Takaful Models in Practice.....	33
2.1.2. Islamic Microfinance.....	35
2.1.2.1. Microfinance Models.....	36
2.2. Non-Market Based Islamic Social Finance Institutions.....	36
2.2.1. Zakat and Ushr.....	37
2.2.2. Waqf.....	38
2.2.2.1. Waqf in Pakistan.....	40
Appendix 2.1: Case Study of Akhuwat.....	40
Chapter 3.....	45
Legal Framework and Outreach of Islamic Social Finance.....	45

3.1. Legal Framework of Islamic Social Finance in Pakistan.....	45
3.1.1. Zakat and Ushr Acts in Provinces.....	45
3.1.2. Legal Framework of Waqf in KP.....	51
3.1.3. Legal Framework for Islamic Microfinance by Financial Institutions .....	53
3.2. Footprint and Outreach of Islamic Social Finance in Pakistan.....	55
3.2.1. Current Collection of Zakat .....	55
3.2.2. Outreach of Microfinance .....	57
3.2.2.1. Outreach of Microinsurance.....	59
3.2.3. Outreach of Waqf.....	61
Appendix 3.1: Estimation of Potential Zakat Collection in Pakistan .....	62
Chapter 4.....	67
Governance and Challenges in Islamic Social Finance in KP.....	67
4.1. Zakat Administration Structure.....	67
4.1.1. Structure and Operations of District Zakat Office .....	68
4.1.2. Role of Group Secretary .....	68
4.1.3. Local Zakat Committees: Formation and Functions .....	69
4.1.3.1. Formation of Local Zakat Committees .....	69
4.1.3.2. Local Zakat Committees Election.....	69
4.1.3.3. Local Zakat Committees Mandate and Work .....	70
4.1.3.4. Issues in Local Zakat Committees .....	70
4.1.4. Zakat Programs and Outreach.....	71
4.1.4.1. Funds Allocation in Different Programs .....	71
4.1.5. Issues in Mustahiq App and Website .....	72
4.1.6. Problems in Zakat Administration .....	72
4.1.6.1. From Muzakki Perspective .....	72
4.1.6.2. From Mustahiq Perspective .....	74
4.1.6.3. From Government Perspective.....	75
4.1.7. Identification and Selection of Beneficiaries .....	78
4.1.7.1. Identification of Beneficiaries: Issues and Problems .....	79
4.1.7.2. Selection of Beneficiaries: Issues and Problems.....	79
4.1.8. Disbursement Process .....	80
4.1.8.1. Disbursement Process: Issues & Problems .....	81
4.1.8.2. Issues Related to Bank .....	82
4.1.9. Auditing Process .....	82
4.1.9.1. Audit Scope.....	83
4.1.9.2. Grievances of Audit Staff .....	83

4.1.9.3.	Problems in Audit Process .....	84
4.1.9.4.	Common Audit Observations.....	84
4.2.	Ushr Governance in Pakistan.....	85
4.2.1.	Challenges in Ushr Collection .....	85
4.2.1.1.	Inadequate Collection .....	85
4.2.1.2.	Incomplete Land Records .....	86
4.2.1.3.	Agriculture Sector is Largely Undocumented.....	86
4.2.1.4.	Rural Centric Production Zones with Limited Agricultural Marketing Infrastructure	86
4.3.	Governance of Waqf in KP.....	86
4.3.1.	Challenges in Waqf Administration.....	87
4.3.1.1.	Inefficiency in Generating Enough Revenues.....	87
4.3.1.2.	Risk of Appropriation .....	87
4.3.1.3.	No Provision in Law for Cash Waqf.....	87
4.3.1.4.	No Significant Public-Private Partnership .....	87
4.3.1.5.	No Orientation of Using Waqf for Social Protection.....	88
4.3.1.6.	No Reporting Standards .....	88
4.3.1.7.	Complete Authority Vested with Chief Waqf Administrator .....	88
Appendix 4.1:	Revisiting the Contemporary Application of Fiqh of Zakat and Waqf.....	88
	Questions Related to Zakat and Ushr.....	89
	Questions Related to Nisab.....	89
	Questions Related to Coverage .....	90
	Questions Related to Zakat and Ushr on Industrial Production.....	91
	Questions Related to Zakat on Corporations .....	92
	Questions Related to Exemptions .....	93
	Questions Related to Zakat on Personal Assets beyond Zaruriyyah.....	94
	Questions Related to Extending the Zakat Net for Consistency .....	95
	Questions Related to Administration .....	96
	Questions Related to Allocation .....	97
	Questions Related to Waqf .....	97
	Questions Related to Zakat-Based Qard al-Hasan .....	98
References.....		100
Chapter 5.....		101
International Best Practices in Islamic Social Finance .....		101
5.1. Overview of Zakat in Malaysia.....		101
5.1.1.	Regulatory and Governance Framework of Zakat .....	101

5.1.2.	Scale of Zakat Collection and Disbursement .....	101
5.1.3.	Tax Incentives on Zakat .....	102
5.1.4.	Zakat on Business .....	103
5.1.5.	Zakat Collection .....	103
5.1.5.1.	Awareness Campaigns .....	103
5.1.5.2.	Collection Methods .....	104
5.1.6.	Zakat Disbursement .....	105
5.1.6.1.	Eligibility Checks.....	105
5.1.6.2.	Asnaf of Zakat.....	108
5.1.7.	Disbursement Schemes .....	108
5.1.7.1.	Disbursement Method .....	111
5.2.	Notable Points in Administration and Practice .....	111
5.2.1.	Public-Private Partnership.....	111
5.2.2.	Use of Technology .....	111
5.2.3.	Reporting and Audit.....	112
5.2.3.1.	Reporting.....	112
5.2.3.2.	Audit .....	113
5.3.	Challenges in Zakat Administration .....	113
5.3.1.	Points of Similarities Between Zakat System in Malaysia and Pakistan .....	114
5.3.2.	Points of Differences Between Zakat System in Malaysia and Pakistan.....	114
5.4.	Overview of Waqf in Malaysia.....	116
5.4.1.	Legal Framework of Waqf in Malaysia .....	118
5.4.1.1.	Allowance of Istibdal of Waqf in Malaysia .....	119
5.4.1.2.	Legal Status of Cash Waqf in Malaysia.....	120
5.4.1.3.	Legal Status of Corporate Waqf in Malaysia.....	120
5.4.2.	Integration of Waqf with Zakat in Malaysia .....	121
5.4.3.	Public-Private Partnership in Waqf Development in Malaysia .....	121
5.4.4.	Housing Ownership through Waqf .....	122
5.4.5.	Challenges in Waqf Management in Malaysia .....	123
5.4.6.	Similarities between Pakistan and Malaysia in Waqf Governance.....	124
5.4.7.	Differences between Pakistan and Malaysia in Waqf Governance.....	124
Chapter 6	.....	126
Policy Recommendations for Using Islamic Social Finance Effectively for Extending Social Protection .....		126
6.1. Policy Recommendations in Zakat Management .....		126
6.1.1. Recommendations in Assessment and Collection.....		126

6.1.1.1.	Enhancing the Coverage of Zakatable Assets .....	126
6.1.1.2.	Enhancing Coverage of Assets in Centralized Collection .....	127
6.1.1.3.	Creating Awareness about Zakat for Enhanced Collection .....	127
6.1.1.4.	Facilitating Seamless Zakat Assessment.....	128
6.1.1.5.	Crowdfunding to Match Funding Gap in Specific Causes.....	129
6.1.1.6.	Introducing Incentives and Differential Treatment for Enhancing Zakat Base .....	130
6.1.1.7.	Establishing a Mechanism for Collection of Zakat from the General Public .....	130
6.1.1.8.	Enhancing Engagement and Utility of Mustahiq App .....	131
6.1.2.	Recommendations in Zakat Administration.....	131
6.1.2.1.	Removing Barriers for Community Engagement .....	131
6.1.2.2.	Creating Data Synergy for Effective Filtering .....	132
6.1.2.3.	Reducing Political Interference.....	132
6.1.3.	Recommendations in Zakat Disbursement.....	134
6.1.3.1.	Using Digital and Fast Mediums of Disbursement.....	134
6.1.3.2.	Introducing Synergies in Programs – Graduation-Based Social Protection .....	134
6.1.3.3.	Introducing Wakalah Program.....	135
6.1.3.4.	Documenting the Economy for Effective Targeting and Profiling .....	135
6.2.	Recommendations for Ushr Management .....	136
6.2.1.	Amendments in the Legal Framework.....	136
6.2.2.	Using Surveys for Assessment.....	136
6.2.3.	Assessing Ushr by Government as Monopsony.....	137
6.2.4.	Introducing Incentives for Ushr Payment to the Government .....	137
6.2.4.1.	Linking Market Access with Ushr .....	137
6.2.4.2.	Linking Subsidies with Ushr.....	137
6.2.4.3.	Tax Incentives for Ushr Payers.....	138
6.2.5.	Strengthening Land Records.....	138
6.3.	Policy Recommendations on Waqf.....	139
6.3.1.	Allowing Private Sector Engagement in Waqf Management .....	139
6.3.2.	Active Waqf Management for Preservation and Growth.....	139
6.3.3.	Encouraging Corporate Waqf .....	139
6.3.4.	Tax Incentives for Creating Waqf.....	140
6.3.5.	Recognition of Different Waqf in Legal Framework.....	140
6.3.6.	Recognition of Cash Waqf in Legal Framework .....	140
6.3.7.	Transparency in Management and Reporting .....	141
6.3.8.	Joint Ventures for Waqf Development .....	141
6.3.9.	Diversify Revenue Streams.....	141



Chapter 7.....	142
Possible Models to Deliver Social Protection Under Islamic Social Finance .....	142
7.1. Mosque-Based Waqf Places for Community Health Services .....	142
7.1.1. Operational Delivery Mechanism .....	143
7.1.2. Points to Consider in Implementation.....	143
7.2. Sadqa P2P Crowdfunding Platforms .....	144
7.2.1. Operational Delivery Mechanism .....	144
7.2.2. Points to Consider in Implementation.....	145
7.3. Voluntary E-Zakat Collection and Disbursement Through Crowdfunding.....	145
7.3.1. Points to Consider in Implementation.....	146
7.4. Mosque-Based Skills Development.....	146
7.5. Integrated Microfinance for Social and Financial Development.....	147
7.6. Role of Mosque in Creating Synergies with Other Programs.....	147
7.6.1. Points to Consider in Implementation.....	149
7.7. Embedding Islamic Social Finance in Sehat Sahulat Card.....	149
7.7.1. Using Takaful.....	149
7.7.2. Using Social Crowdfunding.....	150
7.7.3. Building Smart Hospitals on Waqf Property .....	150

## Acknowledgements

Alhamdulillah, this extensive study has concluded successfully yielding this report based on the year-long activity. All praise to Allah (swt) Who enabled us to contribute our bit to provide evidence-based, well deliberated policy input to the relevant authorities via GIZ on the various modes of Islamic social finance that can effectively help provide social protection to the vulnerable segments of our populace.

The study was ably led by one of the most active researchers in Pakistan on the subject Dr. Salman Ahmed Shaikh, as Principal Investigator. The contribution of Dr. Anwar Shah, as Co-Principal Investigator, and Wali Farooqi, the project's coordinator was instrumental in the successful completion of this project.

The effective execution of the project would not have been possible without the expertise and support of our knowledge partners. In particular, we would like to acknowledge and thank the support provided by Council of Islamic Ideology (CII) in accessing the seminal reports and literature on Zakat and Ushr as well as providing detailed answers to our queries related to Zakat, Ushr and Waqf in Islamic jurisprudence. Our gratitude goes to Prof. Dr. Qibla Ayaz, Chairman CII, Dr. Hafiz Ikram-ul-Haq, Secretary CII, and the research scholars of CII who guided us in this project. The rich input provided through focus group discussions, roundtables and written responses to our comprehensive questionnaire on Zakat and Ushr proved to be highly useful in writing and framing our recommendations.

Furthermore, scholars from different schools of jurisprudence provided invaluable insights during the project which ensured a holistic perspective in this study.

We would like to acknowledge and thank the Zakat and Ushr Department of Punjab, especially former Secretary, Zakat and Ushr, Babar Aman Babar, Zakat Administrator, Muhammad Sajjad Babar, and Additional Secretary Auqaf and Religious Affairs Department, Ahmad Afnan for their valuable support in data collection and insights shared in focus group meetings.

We would also like to acknowledge the research and logistical support provided by Zakat and Ushr Department of Khyber Pakhtunkhwa, especially former Secretary, Zakat and Ushr Ms. Nasheeta Maryam Mohsin, Additional Secretary Zakat Jehanzeb Khan, Deputy Secretary (Ushr) Syed Mubashir Raza, Deputy Director IT Muhammad Azam and Section In-charge (ZMIS) Jameel Afridi. Their valuable support in data collection, insights shared in focus group meetings and logistical support provided to visit and meet the administrative setup at district and local Zakat committee levels helped in understanding the issues in a holistic way for informed policy suggestions.

We are also indebted to our global partners in this project, iWAQF International Waqf Action Council. Dato' Dr. Mohd Ghazali Md Noor, Chairman iWaqf, Dr. Ridzwan Bakar, Director Yayasan Universiti Multimedia and Ustaz Dr. Mohd Syakir, lecturer at Kolej Professional Baitulmal provided invaluable support in meeting the stakeholders of Zakat and Waqf administration in different states of Malaysia. Without the logistical, technical and diplomatic

support provided by iWaqf, it would not have been possible to collect invaluable data from different states of Malaysia including Kedah, Penang, and Federal Territories of Malaysia. We are also grateful for the generous sharing of information by all the respective colleagues who took time out to participate in focus group meetings held in Kedah State, Penang State, Putrajaya and Kuala Lumpur.

We also thank the working group members who attended the focus group meetings, roundtables and also provided time for in-person meetings to understand the issues better and benefit from shared expertise and insights.

We would also like to thank the internal team at Institute of Policy Studies (IPS) which provided the technical, research, logistical and secretarial support to effectively carry out different research activities related to the project.

Lastly, we would also like to thank the support partners, German Agency for International Cooperation (GIZ) which took interest in the area of harnessing the potential of Islamic social finance for ensuring social protection in Pakistan and provided financial sponsorship to carry out the project. Mohammad Mustafa Khan, Technical Advisor-Social Protection at GIZ, took this initiative to explore the potential of Islamic social finance for social protection and this project was successfully completed through joint efforts.

We hope that the efforts of the core research team and the local and global partners will have paved the way for policy dialogue to enhance the role and effectiveness of Islamic social finance institutions in enabling social protection of the masses in Pakistan.

Naufil Shahrukh  
Project Lead/GM Operations  
Institute of Policy Studies  
Islamabad, Pakistan

## Message from GIZ

On behalf of the German Federal Ministry for Economic Cooperation and Development (BMZ), the Support to Social Protection – Social Health Protection (SP-SHP) project is implemented by the Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH. The project is supporting the federal and provincial (Punjab and Khyber Pakhtunkhwa) governments of Pakistan for strengthening social protection systems at the national/sub-national level. GIZ (SP-SHP) is providing technical assistance to GOP within the social protection sector in areas of policymaking, strategy development, operational research for improving evidence-based decision-making, capacity development for effective implementation, and coordination of social-protection programs.

Islamic social finance is an umbrella term for various institutions and tools within the Shari'ah-Islamic legal framework that can be used for extending social protection to the poor and vulnerable, consequently contributing towards achieving the broader objectives of poverty alleviation, equitable growth, and sustainable economic development. Various institutions of Islamic social finance such as Zakat and Ushr, Waqf, Sadaqah and Bait-ul-Mal have historically been used by Islamic communities for helping the poor and vulnerable, incapacitated, those suffering from distress (due to health or economic shock, disaster, etc.). In addition to the state, families and communities have an important role in achieving the true spirit of Islamic social finance.

Islamic social finance has huge potential for contribution towards achieving the Sustainable Development Goals (SDG), i.e. No Poverty, Zero Hunger, Good Health and Wellbeing, Quality Education, Decent Work and Reduced Inequality. This potential, however, remains largely untapped. The Islamic Development Bank has estimated that between \$230 billion and \$560 billion is given in Zakat each year globally. Similarly, in the case of Pakistan, revenue from Zakat could reach 3-4% of the GDP at its maximum potential – potentially providing governments and communities huge alternate sources of investments for meeting a range of development needs. This becomes even more important with the realization that the funding gap to attain the SDGs cannot be closed by traditional sources of financing, i.e. through government funding and development aid.

Through its well-defined and accurate targeting criteria (eight categories of those eligible for receiving it), Zakat has tremendous potential for providing emergency relief to the population in the aftermath of crisis, when it is so important to crowd-in financing from public and private sources to reach the most vulnerable and affected communities. Similarly, Waqf (endowment) is an excellent tool for building resilience through institutions, infrastructure, and permanent sources for funding.

Establishing efficient and transparent systems for Islamic social finance, however, requires ambitious reforms at the policy, legislative as well as operational levels. This includes introducing improved institutional arrangements and governance structures, standards and SOPs for effective management of Zakat, Waqf, Bait-ul-Mal (social protection fund) and other Islamic social finance tools.

Launch of this report on ‘Islamic Social Finance for Social Protection in Pakistan’ by the Institute of Policy Studies is the first-ever seminal work on the topic in the country. The data collection process involved extensive literature review as well as consultations and deliberations with a wide range of stakeholders including religious scholars, government departments, academia, think tanks, civil society, practitioners, etc. Based on in-depth review and analysis of the status quo in the country as well as that of best practices in other countries, the study has produced concrete recommendations for reforms in Islamic social finance.

I would like to congratulate IPS and their research team for this achievement and would like to urge them to continue working in further building this important area of knowledge and practice.

Mohammad Mustafa Khan  
Technical Advisor  
Social Protection-Social Health Protection  
Deutsche Gesellschaft für  
Internationale Zusammenarbeit (GIZ) GmbH

## Executive Summary

The Islamic welfare approach, being a multidimensional phenomenon, not only focuses on the spiritual well-being of the individuals but also their economic sustainability. Need fulfillment of every citizen of the state is an important goal to achieve one of the ultimate objectives of Shari'ah, i.e. *Hifz-ul-Maal*, out of the five primary objectives. For this, Shari'ah promotes the circulation of wealth and resources among all sectors. Various products of Islamic social finance, whether these are financial in the form of Zakat and Ushr or all other institutions like Waqf, inheritance, etc. also ensure the distribution of wealth. In Pakistan, Takaful and Islamic microfinance are two major market-based Islamic social finance products, though they provide very limited coverage. Non-market based products include voluntary charities, as well as Zakat, Ushr, and Waqf.

The institution of Zakat (lit. purification), often mentioned alongside Salat (prayer), is a redistribution mechanism that can be fully optimized through the implementation of a centralized system that ensures smooth and efficient collection and distribution of Zakat funds. There is room for serious efforts to improve Pakistan's Zakat as well as Ushr and Waqf systems to help alleviate poverty. Problems such as technical and budgetary constraints, outdated legal framework, complicated, ineffective, overlapping institutions, etc. require a systematic approach to social protection that focuses on creating linkages among the pillars of social protection, i.e. social assistance, social insurance, labor market programs, and social services.

The underlying study, carried out by the Institute of Policy Studies in collaboration with GIZ, aimed at understanding the social security mechanisms in Islam, understanding and identifying various problems and obstacles encountered in collecting and institutionalizing Zakat, Ushr, and Waqf, exploring ways to tackle these issues, and finally proposing policy steps for reforming the existing system. The study was conducted by reviewing and analyzing secondary data, documents, regulations, and extant literature on Islamic social finance to foster welfare with Islamic spirit.

The scope covered documenting and exploring primary information to unearth footprint, coverage, hurdles, and policy suggestions regarding the current and prospective role of Islamic social finance institutions through interviews and focus group meetings with relevant stakeholders in two provinces of Pakistan, i.e. KP and Punjab.

The study also covered the Malaysian model of Zakat and Ushr. For this purpose, the research team visited three cities of the country to meet different governmental and private organizations and study the current successful Malaysian model of Zakat and Ushr.

The obtained data sets were analyzed through qualitative and quantitative techniques, including various statistical, analytical, and exploratory tools, including graphical and tabular presentations, case studies, and summaries.

Even though the potential of Zakat collection in Pakistan, as explored by the study, is very high, the actual collection by the government is meager, with an almost non-existent voluntary

collection. This is mainly due to the lack of awareness about the rules of Zakat, the prevailing lack of trust between the payers and the collecting agencies in terms of transparent utilization of funds, the issue of Tamleek, and the absence of detailed annual reports by the Zakat Department.

Furthermore, decentralization due to the 18th Constitutional Amendment, allowance of affidavit submission granted to everyone, deficiencies in Zakat committees, i.e. no diversification and passive members, small number of committees, and political selection in certain cases, makes it difficult to collect a handsome amount of Zakat, which ultimately results in ineffective coverage due to lack of funds.

This nominal amount of Zakat is then used for selected beneficiaries as priority is given to the disabled, widows, and orphans. Lastly, there are issues in the disbursement of funds through banks such as transaction fees and non-cooperative bank staff. Though the launch of the Mustahiq app by the KP government is an excellent initiative, it lacks provision of forms in local languages, form submission through the app, and features that facilitate the Muzakki.

Regarding Ushr, it is not very common in Pakistan. There is inadequacy in the collection of Ushr at the government level due to incomplete and undocumented land records, poor agricultural marketing infrastructure, and lack of government strategies regarding Ushr payment. A motivational strategy might include stamping products with 'Ushr-payer' logos by the authorities, taking the example of Malaysia.

Waqf, managed by the Auqaf Department and Religious Affairs in the provinces, is also largely passive in Pakistan as compared to other countries like Malaysia. Currently, the institution of Waqf is not properly utilized and fails to generate adequate revenues. The main focus of the department is on maintenance rather than using the properties for social protection. Moreover, there is no legal framework for Cash Waqf, Family Waqf, and Corporate Waqf. Hamdard Laboratories is the only example of Corporate Waqf, while Cash Waqf is non-existent.

In Malaysia, Zakat system is decentralized to the state level. Each state has State Islamic Religious Councils (SIRCs) which look after the administration of Zakat and Auqaf. The administration of each Zakat institution is subject to the authority of the SIRCs. There are specific laws and enactments which regulate the Zakat system; however, Fatwas of the SIRCs have an important role in running the affairs of Zakat as well. However, there are agencies known as Jabatan Wakaf, Zakat dan Haji (JAWHAR) responsible for planning, implementing, monitoring, and coordinating the development of Waqf, Zakat, Mal and Hajj/Umrah institutions to function more effectively in the socio-economic development of the Ummah.

Keeping all these findings in view, the current report suggests that, first of all, the legal frameworks for Zakat, Ushr, and Waqf should be revised; coverage should be extended to the assets currently not covered by the Zakat and Ushr Act, 2011; land records should be updated to extend Ushr coverage; and laws for Family, Cash, and Corporate Waqf should be added.

To sensitize people towards the payment of Zakat and Ushr, and promote Waqf, there should be awareness campaigns through digital and electronic media, as well as through different on-ground sessions by utilizing community mosques. Different incentives and subsidies could also be provided to the payers of Zakat, Ushr, and Waqif.<sup>1</sup>

The existing system needs to be digitized for ease of payment and receiving of Zakat, which will also ensure transparency. A proper digital mechanism of the collection and payment of Zakat receivables should be established using various fintech solutions. Similarly, the websites and mobile applications should be redesigned with enhanced and additional features like Zakat calculators, Fiqh-related issues, etc. in a user-friendly manner. Other electronic means, such as telephone helplines and WhatsApp chats, should be created which can help people in resolving Zakat-related queries.

For an increase in revenues, there should be synergies across various Zakat collecting organizations, developing Waqf properties for diversified investments, and transparency in the distribution mechanism, which can be achieved by depoliticizing the selection process of the local Zakat committees, and proper publishing of detailed annual reports.

Finally, various community service programs can be introduced by using a mix of skilled and educated volunteers, local Zakat committees, digital platforms, and mosques.

---

<sup>1</sup> A person who establishes Waqf



## Foreword

It is said that man is a social animal. Regardless of how complete and comprehensive this definition of the best creature (Ashraf al-Mukhlūqat) ‘the man’ is, the fact is that it is not possible for man to live on his own. It is not only his psychological need to live with other human beings, but it is also impossible for him to survive without any ‘social security’ system in this world. Nature has provided for him a system in the form of the mother’s lap from day one and permanently in the form of the institution of the family, which in its ideal form, ensures social protection throughout life.

The entire world of humanity is also like a family, and here too, the ideal situation would be that all its members should take care of each other’s social protection needs. Indeed, some efforts are being made for this purpose globally. These efforts also include the goals, first set in the form of Millennium Development Goals in 2000 and later Sustainable Development Goals in 2015, which target by 2030, among others, complete eradication of poverty and hunger from the world, provision of health and education facilities, and reduction in inequality. However, it is a sad reality that progress towards these targets seems relatively slow and in some cases even negative, e.g. hunger. The FAO’s ‘State of Food Security and Nutrition in the World 2022’ report affirms that the world is moving backwards in its efforts to end hunger, food insecurity and malnutrition.

A look at the situation in Pakistan shows there has been a marginal improvement in the social security indicators statistically, but in terms of substance, the condition is not ideal.

The situation would probably have been much worse if there had been no public activism in Pakistan in light of the Islamic teachings of Sadaqat Wajiba and Sadaqat Nafala regarding social security. The fact is that many private initiatives are playing a significant role in social protection in Pakistani society in addressing the issues of poverty, hunger, education, health, and employment.

However, no matter how much private initiatives increase, they cannot be a substitute for a system planned and formulated at the national level while considering the needs and priorities. It is a sad fact that despite the constitutional provisions and initial legislation and formulation of a system in this regard in the 1980s, the government has failed to utilize the potential in society in light of Islamic teachings. As a result, the annual collection of Zakat has been fluctuating and it was around Rs. 10.8 billion in 2022, according to the SBP Annual Report. In most cases, it is based only on the mandatory deductions collected under the law on bank deposits, shares, etc. The amount of voluntary deposits in the total mix was barely 0.03% in 2022, the lowest in the last six years.

In this situation, the benefits and blessings intended to be achieved by implementing the collective form of this system given by Islam for social security are not being attained.

In this background, the current study conducted by the Institute of Policy Studies with the collaboration of GIZ is majorly based on the review of Zakat & Ushr and Waqf laws, the system

designed in their light and implementation of this system in the Khyber Pakhtunkhwa and Punjab provinces. The groundwork for this review included direct meetings, focus group discussions with stakeholders and users of the system at various levels, and a study of the systems prevalent abroad, particularly in Malaysia. In addition to benefiting from the opinions of different schools of thought, constant consultations were held with experts associated with the Council of Islamic Ideology. We are grateful to the Chairman, Dr. Qibla Ayaz, and Secretary, Dr. Ikram-ul-Haq of the Council of Islamic Ideology, and their entire team for the help provided.

The study has once again made it clear that if the system of Zakat and Ushr (and other social security institutions) is implemented cohesively with integrity, good faith, and professionalism, it will help in substantially reducing, if not eliminating in the short period, social insecurity. Besides, the resultant prospects of economic activity will also assist in resolving many other problems the economy faces. The fact is that there is a general desire and support for such a system in Pakistani society with an Islamic background; the problem is building trust in the relevant laws, structure, and implementation system. Hopefully, the suggestions given in this study will help ease this journey.

Khalid Rahman  
Chairman  
Institute of Policy Studies  
Islamabad, Pakistan

## Chapter 1

# Social Protection and the Islamic Welfare Approach

### 1.1. An Introduction to the Islamic Welfare Approach

*Falah* (welfare) is an all-encompassing objective envisaged in Islamic worldview for human beings. In managing the affairs of this world, the principles laid down by Islam provide the foundations of a system which ensures the establishment of a welfare society, whose first and foremost duty is to provide necessities of life to its citizens.

Renowned Muslim economist, Umer Chapra, in his book *The Islamic Welfare State and its Role in the Economy* mentions some of the essential functions of the Islamic welfare state with respect to the economy. These include:

- 1) To eradicate poverty and create conditions for full employment and a high rate of growth;
- 2) To promote stability in the real value of money;
- 3) To maintain law and order;
- 4) To ensure social and economic justice;
- 5) To arrange social security and foster equitable distribution of income and wealth;
- 6) To harmonize international relations and ensure national defense.

Chapra highlights that it is mandatory for an Islamic state to make positive efforts for achieving a good life (*Hayat-e-Tayyaba*) and welfare (*Falah*) for its people both spiritually as well as in the form of provision of ease and alleviation of hardship, generation of prosperity, and ensuring freedom from moral corruption, hunger, fear and deprivation. Hence, all institutions including the policies of the state should cater to the welfare of everyone. In Islamic jurisprudence, this principle is used with the name of *Maslaha*.

Mere abundance of wealth or its accumulation is not the supreme goal in Islamic society. Fundamentally, what is important is need fulfilment of every citizen of the society regardless of color, caste, creed and race.

A society with equitable distribution of resources where the needs of the members of the society are met sufficiently with equitable opportunities of growth is better than a society with more abundant resources, but where wealth and resources are so much inequitably distributed that a great number of people suffer from poverty and hunger and unequal distribution of income. The fulfilment of needs of individuals and society necessitates the state to play a vital role in

the economic system of Islam. The UN's goals one (zero poverty) and two (zero hunger) among the seventeen Sustainable Development Goals (SDGs) also emphasize poverty eradication and ending hunger.

### 1.1.1. Distribution of Wealth

Islamic economic principles are against concentration of wealth within a few hands. Rather, Islamic principles encourage resources to flow widely in broader segments of the society. In the context of circulation of wealth, Islam has a very comprehensive concept of redistribution of income and wealth which centers on forbidding all forms of interests and interest-based transactions, and recommending mandatory charity in the form of Zakat and voluntary charity in the form of Sadaqat. The institution of Zakat and Ushr constitutes obligatory charity through which resources flow from the richer segments of the economy and society to the poorer segments of the society. In addition to these mandatory levies, Islam repeatedly encourages the well-off people in the Muslim society to generously contribute voluntarily to charities.

Zakat is a 2.5% charge on certain forms of wealth which remains in one's possession for a lunar year. The forms of wealth include currency, gold, silver and all held-for-trade real, financial, movable, immovable, tangible and intangible assets. On the other hand, Ushr is a charge on the agricultural produce of land levied on the Muslims at the rate of 10% if the land is irrigated by rainfall and at the rate of 5%, if the land is irrigated artificially.

Zakat, Ushr, Waqf, and the laws of inheritance are various Islamic mechanisms that ensure circulation of wealth.

Furthermore, Waqf is another institution which ensures dedicated public social safety nets which provide beneficial services to the public at large on permanent basis. Islamic laws of inheritance also ensure wide distribution of resources from the wealth of every single deceased person. This redistribution at individual level in every Muslim household ensures intergenerational redistribution of resources.

This one-to-many redistribution of resources from the wealth of a single deceased person to a wide array of relatives checks wealth concentration at the micro-level in every household. These redistributive tools can help in making progress in achieving the UN's SDG ten, which is focused on reducing income inequality.

### 1.1.2. Principle of Self-Reliance

Islamic principles discourage idleness on the part of labor. The various sayings of the Prophet Muhammad (PBUH) encourage engagement in gainful economic pursuits to avoid being a 'taker' rather than a 'giver'. It is the responsibility of the Islamic state to ensure decent work opportunities for its citizens. The UN's SDG eight is also about decent work opportunities and growth. The government should play its role in encouraging and engaging all citizens with the capacity to work, to take up gainful means of livelihood leading to sustained earnings and self-sufficiency.

Islam enjoins upon the individual to earn his livelihood by labor. The Prophet (PBUH) says: “No one ever eats food better than that which he earns by the labor of his hands...”<sup>2</sup> It is the responsibility of the state to take all possible measures to ensure that its citizens find suitable jobs for which they are qualified.

Narrated Anas ibn Malik: A man of the Ansar came to the Prophet (PBUH) and begged from him. He (the Prophet) asked: Have you nothing in your house? He replied: Yes, a piece of cloth, a part of which we wear and a part of which we spread (on the ground), and a wooden bowl from which we drink water. He said: Bring them to me. He then brought these articles to him and he (the Prophet) took them in his hands and asked: Who will buy these? A man said: I shall buy them for one dirham. He said twice or thrice: Who will offer more than one dirham? A man said: I shall buy them for two dirhams. He gave these to him and took the two dirhams and, giving them to the Ansari, said: Buy food with one of them and hand it to your family, and buy an axe and bring it to me. The man then brought it to him. The Apostle of Allah (PBUH) fixed a handle on it with his own hands and said: Go, gather firewood and sell it, and do not let me see you for a fortnight. The man went away and gathered firewood and sold it. When he had earned ten dirhams, he came to him and bought a garment with some of them and food with the others. The Apostle of Allah (PBUH) then said: This is better for you than that begging should come as a spot on your face on the Day of Judgment. Begging is right only for three people: one who is in grinding poverty, one who is seriously in debt, or one who is responsible for compensation and finds it difficult to pay. (Abu Dawud: Sunan, Kitab al-Zakat, Bab Ma Tajuz fih al-Masalah).

## 1.2. Zakat – The Fundamental Social Protection System in Islam

Zakat is one of the fundamental pillars of faith in Islam. It is a social protection tool for the welfare of the poor, underprivileged and vulnerable members of Muslim society. It provides the basis of the concept of welfare society through solving problems such as poverty, indebtedness and inequitable income distribution in a Muslim society, at family, community and state level.

The word Zakat in Arabic means purification and development, i.e. to help something grow up smoothly and develop without obstruction. It entails:

- i) the act of purification of wealth by taking out a portion thereof and spending it in charity in way of Allah,
- ii) self-purification through the act of worship,
- iii) as well as purification of other fellow members of the society in general.

Zakat is not only designed for the welfare of society, but for the spiritual advancement of the one who pays Zakat, for the improvement of social conduct of the individual and the society as a whole.

---

<sup>2</sup> Bukhari, Kitab-ul-Buyoo’ (Book of Transactions), Hadith: 2072.

It is one of the fundamental principles of Islam upon which the Muslims' salvation in this world and the hereafter depends. Salah and Zakat have been mentioned side by side at 37 different places in the Holy Qur'an mostly where the attributes of a worthy believer are described. Allah SWT says in the Holy Qur'an:

“And We made them into leaders to guide people in accordance with Our command, and we inspired them to good works, and to establish prayers and to give Zakat. They worshipped us alone.” (Al Anbiya, V: 73)

“Yet all that they had been commanded was that they serve Allah, with utter sincerity, devoting themselves exclusively to Him, and that they establish prayer and pay Zakat. That is the right faith.” (Al Bayyinah; V: 5)

“This is the Book of Allah, there is no doubt in it; it is a guidance for the pious, for those who believe in the existence of that which is beyond the reach of perception, who establish prayer and spend out of what we have provided them.” (Al Baqarah; V: 2-3)

“They [believers] are those who establish prayer and donate from what We have provided for them.” (Al Anfal; V: 3)

“Only Allah, His messenger, and those who believe and who establish prayer, pay Zakat, and bow down (before Allah) are your allies.” (Al Maidah; V: 55)

“But if they repent and establish prayers and give Zakat, they are your brethren in faith.” (At Tawbah; V: 11)

Zakat is one of the three primary duties and responsibilities of the Muslim nation as a precondition for their success and victory.

The Qur'an states:

“those who, were We to bestow authority on them in the land, will establish prayers, render Zakat, enjoin good, and forbid evil. The end of all matters rests with Allah.”

(Al Hajj, 41)

In the following verse, it is declared as to what are one of the three primary duties and responsibilities of the Muslim nation as a precondition for their success and victory:

“those who, were We to bestow authority on them in the land, will establish prayers, render Zakat, enjoin good, and forbid evil. The end of all matters rests with Allah.” (Al Hajj; V: 41)

Similarly, Allah SWT says:

“You shall not attain righteousness until you spend (for the sake of Allah) out of what you love. Allah knows whatever you spend.” (Aal e Imran; V: 92)

“Establish prayers and pay Zakat and obey the messenger so that mercy maybe shown to you.” (Al Nur; V: 56)

This redistribution mechanism is meant to bring efficiency and growth in the economy and uproot poverty gradually and steadily. It requires that redistribution of resources must therefore be addressed with serious and effective policy tools.

In the event that an individual is unable to achieve economic independence from markets alone, then social security is one of the policy frameworks of Islam for eradicating absolute poverty. The concept of brotherhood and solidarity ensures wide coverage of social security and social

protection to every citizen. The concept of the government's responsibility for provision of basic subsistence compels the state to have an adequate system of social security and social protection.

### 1.2.1. Importance of Organized System for Collection and Distribution of Zakat

Islam stresses the importance of having an institutionalized system for the collection and distribution of Zakat. The role of government in an Islamic state regarding the collection and distribution of Zakat and Ushr is essential. Having a proper mechanism to administer Zakat is one of the most fundamental constitutional duties of an Islamic state, and force can be used against the evaders.

“(O Prophet)! Take alms out of their riches and thereby cleanse them and bring about their growth (in righteousness) and pray for them. Indeed, your prayer is a source of tranquility for them.”  
(Al Tawbah; V: 103)

In case of absence of such a government or when such a government is negligent, i.e. there is no official arrangement for the collection and distribution of Zakat, it remains obligatory for the Muslims as a community to ensure observance of Zakat and to have a proper organized structure for this purpose. As such every Muslim who is in position of the prescribed amount of wealth is duty-bound to pay Zakat regularly. The experience of the early Muslim history proved that when Zakat was rightly collected and distributed to its deserving recipients, it led to the alleviation of poverty in that society.

Zakat was collected and distributed by the state during the time of the Holy Prophet (PBUH) and Al Khulafa ar-Rashidun as well as by all successive Muslim governments. It is therefore obligatory for the Muslim community to have a proper setup for the collective management of Zakat in order to reap the real dividends of this revolutionary system. As a general principle, the responsibility for collection and distribution of Zakat should rest with the provinces, with the center enjoying the powers to divert the surplus of one province to a Zakat deficient province or area. The center should also have the power to launch institutions or schemes of social welfare in the way of Allah and to mobilize emergency relief operations within the country or abroad.

## 1.3. The Context of Pakistan

Developing countries continue to face poverty, although many of these states take serious initiatives for alleviating this issue. In such countries, social protection is used as a policy framework employed to address poverty and vulnerability.

Social protection is considered a key component of development policy. Social protection, as defined by the United Nations Research Institute for Social Development, is concerned with preventing, managing, and overcoming situations that adversely affect people's well-being. Beyond its role as a policy framework addressing poverty and vulnerability, social protection embodies and extends alternative approaches to economic and social development. There is

growing evidence today that effective social protection systems contribute to multi-dimensional impacts such as poverty reduction, human capital development, improved livelihoods and labor market participation as well as stimulating economic growth.

Pakistan has one of the most significant Muslim populations in the world (approximately 220 million). The Government of Pakistan is trying to fulfil its objective of a welfare state through different social protection schemes and poverty alleviation programs, the most popular being Benazir Income Support Program (BISP), which was also branded as Ehsaas for some time.

This program was launched with the objective to reduce inequality, invest in people, and lift lagging districts. It aims for the creation of a ‘welfare state’ by countering elite capture and leveraging 21st century tools such as using data and technology to create precisely targeted safety nets; promoting financial inclusion and access to digital services and supporting the economic empowerment of women.

The budgetary allocation for the BISP program for the year 2021-22 was Rs. 250 billion, which was enhanced to Rs. 364 billion for the fiscal year 2022-23. Millions of people are supported through this program. As a result of its successful implementation, many deserving families and individuals are getting socially protected one way or the other.

In respect of providing social protection to the citizens, Pakistan Bait-ul-Mal has also been contributing towards poverty alleviation programs for many years by aiding destitute, widow, orphan, invalid, infirm and other needy persons, as per eligibility criteria approved by the Bait-ul-Mal board. This institute has assistance programs for those who are outside the domain of labor market and are extremely poor and considered marginalized segments of the society. Assistance is provided through in-kind or unconditional cash transfers.

In Pakistan, under the law, the task of Ushr assessment and collection has been assigned to the provincial revenue departments. This institution is yet to achieve its potential of becoming a major source of social protection by providing assistance to deserving individuals, especially in the rural areas. Special efforts should be made for the optimum collection of Ushr.

Likewise, ever since nationalization, the private sector has refrained from institutionalizing Waqf beyond the centers of mosques, Madaris and shrines. The regulatory framework also lacks clarity and provision to institutionalize mobilization of welfare resources through Waqf and to manage it flexibly and transparently within the private sector.

Although, the Social Welfare Department is performing multiple welfare functions in Pakistan, there are significant gaps in the structure and function of the department such as:

- ❖ The department has a limited budget and suffers from staffing and technical resource constraints.
- ❖ The legal framework under which the non-profit sector functions is outdated.
- ❖ The work is overly complicated and grossly ineffective.



- ❖ There are multiple overlapping institutions and programs with limited synergies.
- ❖ Changes in governance structures and their improper implementation lead to significant conflicts between the Social Welfare Department officers at different levels.

The department needs to develop strategies to ensure that all social welfare programs of public and private sectors are adequately coordinated to avoid wastage of limited resources, and to ensure systematic delivery of social services to all deserving people.

#### 1.4. Need for Social Protection in Pakistan

Around one-third of Pakistan's population continues to live in poverty, corresponding to some 70 million poor individuals. According to a recent report by the World Bank, the social protection programs in Pakistan have limited coverage, covering approximately 5% of the total population as compared to a multi-dimensional poverty rate of about 38%. The government needs to have some adequate institutional arrangements for multi-sectoral orientation of social protection agenda, employing the available funds from Zakat/Ushr and other sources of revenue.

According to a recent report by the World Bank, the social protection programs in Pakistan have limited coverage, covering approximately 5% of the total population as compared to a multi-dimensional poverty rate of about 38%.

Past experience with social welfare programs, such as Zakat and Bait-ul-Mal, shows that poorly designed programs can divert social transfers away from their most deserving recipients. The mechanism of collection and distribution of Zakat needs to be appropriately addressed. There is a need to develop a transparent system, in order to remove the present trust deficit between the government and the citizens on this matter. The state-level Zakat system in Pakistan – initiated through the Zakat & Ushr Ordinance, 1980 and later devolved to the provinces after the 18th Constitutional Amendment in 2011 – is limited in funds and resources and hence ineffective in creating a major impact.

Since the passing of the landmark 18th Constitutional Amendment, a substantial portion of social welfare provision, including healthcare and education, has been devolved to the provinces. As a result, there has been an expansion in provincial social welfare programs reflecting regional priorities. The provinces simply do not have the resources, capacities or existing programs in place to address the challenges for welfare provision.

The concerns about insufficient federal government support to the provinces in respect of providing social security are serious. Numerous governments in Pakistan have expressed the desire to build a welfare state, but those verbal appeals seem worthless unless supported by concrete steps to expand the scope of Pakistan's limited existing safety nets.

The government's response to the multiple challenges faced by the citizens is broad and extensive but is characterized by lack of coordination and lack of a systems-based approach. A systems-based approach to social protection calls for developing national and sub-national

social protection strategies whereby different programs operating under various administrative domains are brought under one overarching policy and strategy framework.

A systems-based approach focuses on coordinating between the four pillars of social protection – social assistance, social insurance, labor market programs and social services – as well as building bridges with other policy areas, both social and economic.

This can be done through creating linkages among various programs within and across each pillar through sharing data and monitoring systems, enrolment, and delivery systems at an operational level while a single entity empowered to coordinate social protection programs across sectors and departments at an institutional level. This becomes more important after the 18th Constitutional Amendment whereby social protection has been devolved to the provinces.

Even at present, Pakistan is facing complex public health, economic and social crises that require attention of policymakers to act decisively and build consensus to develop well-designed programs that complement rather than compete with the existing welfare programs at both the federal and provincial levels.

Despite its well-known significant role in a Muslim economy, the institution of Zakat remains unaddressed in Muslim nations. Some of the reasons include the following:

- ❖ Juristic differences among Muslims on the means and procedures of Zakat and Ushr assessment, collection and distribution.
- ❖ Muslim states lack the political will to establish systems for the collection and distribution of Zakat.
- ❖ The wealthy citizenry often prefers to keep Zakat in the private domain so that their wealth is not externally audited.
- ❖ People are less inclined towards payment of Ushr and there is no organized system for its collection and assessment.

At the institutional level, the management of Pakistan Bait-ul-Mal and Zakat indicates lack of a coherent strategy to employ social safety nets at the government level as well as a lack of coordination. Although the two programs are formally linked, the government approaches each program independently. While, the disbursement of Zakat is decentralized, Pakistan Bait-ul-Mal is maintained at a centralized level. The provincial, district, and sub-district governments hardly play any role in Pakistan Bait-ul-Mal programs, a link that must be created for better inter-tier coordination.

In the final analysis, it is the state which is supposed to take up the responsibility of transforming Pakistan from a poor, underdeveloped and economically dependent state to a welfare state where the resources are optimally used for the betterment of the people. There is

a need to develop long-term programs that will address the pressing health, employment and hunger concerns for the citizens of Pakistan.

The costs of ignoring current welfare challenges will be devastating for Pakistan's most marginalized citizens, unless new and ambitious public policy measures are taken. Hence, there is a need to evaluate the federal and provincial level policies, legislation, and administration in Pakistan vis-à-vis Islamic social finance. There is also a need for evidence-informed discussion among experts and all relevant stakeholders on these issues to resolve them with consensus and to design an efficient Islamic social finance system utilizing the potential of Zakat, Ushr, Waqf, Takaful and Qard al-Hasan to mobilize resources and then allocate them in priority programs in a targeted, systematic, transparent and efficient way.

At present, the government is facing a challenge to have an increased collection of Zakat and Ushr and revitalize dormant institutions like Waqf, which could only be achieved after removing the trust deficit between the government and the public. The immense potential of Zakat, Ushr and Waqf in a Muslim nation like Pakistan, if converted into an efficient state policy, can prove to be a potent vehicle for poverty alleviation and distributive justice.

The immense potential of Zakat, Ushr and Waqf in a Muslim nation like Pakistan, if converted into an efficient state policy, can prove to be a potent vehicle for poverty alleviation and distributive justice.

As stated earlier, redistribution of resources has a great importance for constructing social protection policies. Redistribution in Islam is primarily intended to serve the goal of need fulfilment and combating poverty. Secondly, it aims at reduction of inequality. Islam has given it clear institutional backing through transfers from the public treasury in addition to the payment of Zakat. The government needs to focus on increasing and managing the supply of redistributable resources, since resources available for redistribution are never enough.

Since they are given free without cost, there is always an excess demand for them. Therefore, targeted disbursement of resources in a transparent way with effective monitoring is vital. This requires strong institutional administration and setup. Moreover, redistribution could have a potentially negative impact on work incentives of both donors and recipients, which may reduce future output. In light of this, the government ought to find ways for decreasing and managing the demand for redistributable resources because in the field of policy, redistribution is not just tax and transfer. It includes policies that improve the quality of human capital, especially through health and educational improvements, as also aimed by the UN's SDGs three (good health and well-being) and four (quality education).

## 1.5. Introduction to the Study

Based on this background, Institute of Policy Studies carried out research with the purpose to evaluate the potential and ways of institutionalizing the above-mentioned tools of enhancing welfare in the Islamic socio-economic framework.

The study focuses on Pakistan in particular, which has 97% majority of Muslims. Several previous studies have found that people in Pakistan are generous in philanthropic giving and religious motive is the strongest reason for such spending (For instance, ‘National Survey of Individual Giving by Aga Khan Development Network’ in 1998 and also ‘Philanthropy in Pakistan’ by Pakistan Center for Philanthropy). Therefore, in the context of Pakistan, it is better to institutionalize socially and culturally favorable tools of welfare enhancement with which people are familiar and in which they have confidence. Such Islamic social finance tools can be used in resource mobilization as well as resource allocation for social protection.

The study further explores ways to incorporate Islamic welfare paradigm and tools into the current social protection system. It analyzes strategies for institutionalizing these tools in the current regulatory and administrative framework and suggests changes for adjustments and reforms in order to assimilate these institutions in the current administrative and regulatory dispensation.

The study conducted careful analysis of data, regulations, relevant reports, extant literature and by documenting on the ground situation by means of interviews and group discussions involving scholars and experts in the field. The research engaged with the relevant stakeholders to identify hurdles, difficulties and ways of improving the institutionalization and delivery of these Islamic social finance tools. The research offers practical recommendations to the federal and provincial governments to build up an adequate social protection system for the citizens within the framework of an Islamic welfare state. This report is a summary outcome and findings of the research project.

Scope of the study includes review and analysis of secondary data, policy documents, regulations and extant literature on Islamic social finance to foster welfare with an Islamic spirit. The scope also covers documenting and exploring primary information to unearth footprint, coverage, hurdles and policy suggestions regarding current and prospective role of Islamic social finance institutions through interviews and focus group meetings with relevant stakeholders in Pakistan and Malaysia.

### 1.5.1. Study Objectives

In order to address the aforementioned problems, research would be carried out to propose practical solutions to the federal and provincial governments. The main objectives of the research would be:

- ❖ To understand the mechanisms of social security in Islam and how Islamic social finance institutions cater to the social protection needs of people.
- ❖ To understand the practical application of Islamic social finance institutions by looking at practices in the national context and also in a global context.
- ❖ To identify the obstacles encountered in institutionalizing Zakat, Ushr and Waqf system in Pakistan in terms of shortfall in funding, scarcity of human resources, lack of regulatory impetus, governance issues, weak outreach, low level of visibility and transparency and limited socio-economic impact as a result.

- ❖ To explore ways to incorporate Islamic social finance institutions into the current social protection system to revitalize and leverage institutions like Zakat, Ushr, Waqf and Takaful.
- ❖ Finally, to suggest policy steps in legal framework, institutional building and reforming existing systems to remove the obstacles identified in the system.

### 1.5.2. Study Questions

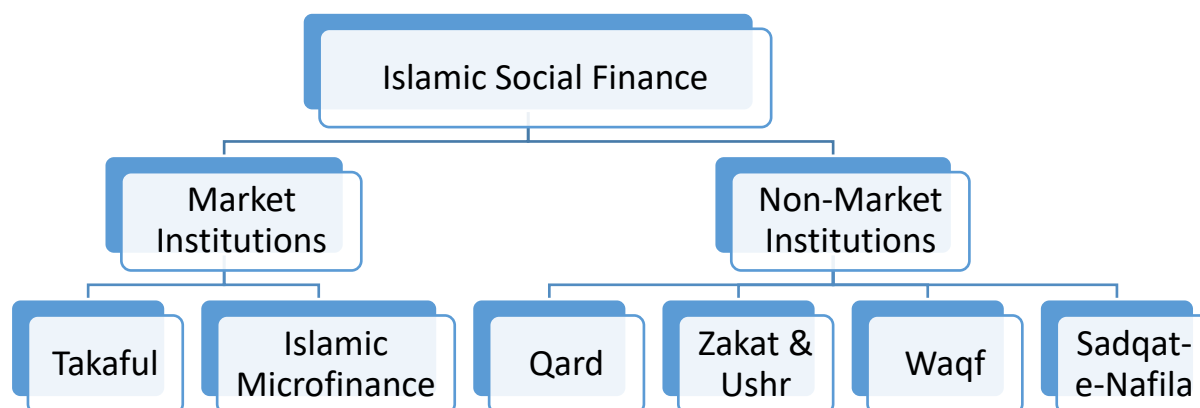
This study answers some major questions regarding the Islamic social welfare program. These questions helped the research group to draft a policy for social protection for the citizens of Pakistan, especially in KP and Punjab.

A few questions which have been researched in this study are as under:

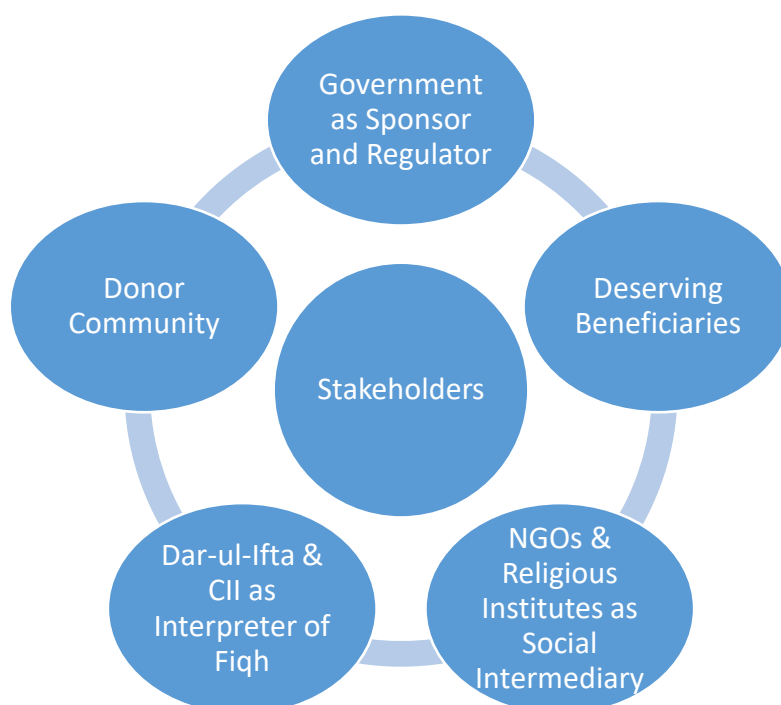
- ❖ What are the institutions and service delivery mechanisms in Islamic social finance for social protection?
- ❖ What is the existing legal and regulatory framework including laws, acts and policies at the level of government regarding Islamic social finance institutions and service delivery mechanisms?
- ❖ What are the recommendations for making the system for assessment, collection and disbursement of Zakat more efficient and effective both from a theoretical and practical perspective at each of the three levels?
  - Legislative Level
  - Institutional Level
  - Operational Level
- ❖ What are the recommendations for having an organized and practical/feasible system for collection and assessment of Ushr in Pakistan's current context?
- ❖ What are the recommendations for institutionalization of Waqf and Sadaqat (voluntary spending for a good cause)?
- ❖ In what ways the current social protection programs can be made compliant with Islamic principles so that there can be increased participation of stakeholders in the system, both in terms of funding those programs and also in using the programs for extending welfare services for the people?

### 1.5.3. Research Design and Methodology

This research was carried out by using both qualitative and quantitative research analysis. First, the institutions and instruments in the Islamic social finance system were identified. Figure 1 shows the instruments in the Islamic social finance ecosystem.

**Figure 1: Islamic Social Finance Ecosystem**

Second, the key stakeholders in the Islamic social finance ecosystem were identified as shown in Figure 2.

**Figure 2: Stakeholders in the Service Delivery Mechanism of Islamic Social Finance**

The government provides the regulatory framework through enacting laws and acts. It performs and facilitates the regulatory and audit function. It also runs social protection programs and funds it through budgetary and administrative support itself or with the help of other arms of the government or NGOs and civil society organizations. Examples of these are various programs under the Benazir Income Support Program, Prime Minister's Health Insurance Scheme, Kamyab Jawan Program, Naya Pakistan Housing Scheme, Employees' Old-Age Benefits Institution and Pakistan Poverty Alleviation Fund.

Donor community includes individual donors residing in Pakistan or overseas, corporate philanthropists, and donor and aid agencies both inside and outside the country. These elements in the donor community provide the necessary funds needed for social protection in Pakistan.

Deserving beneficiaries are individuals in need of help or caretaker organizations working on the welfare of such people in health, education, capacity building, rehabilitation and relief.

NGOs and religiously oriented establishments and institutions, such as mosques and shrines, act as social intermediary connecting the donor community and deserving beneficiaries outside the ambit of government to plug the trust deficit and gaps in the coverage of government-run programs of welfare and social protection. Communities which feel that their own limited size of dispersed population and resource constraints in the government-run welfare programs may not enable them to ensure social protection within the community, endeavor to have community-based social protection service delivery mechanisms to ensure effective coverage of their community members.

Finally, Ulema in Dar-ul-Ifta and Council of Islamic Ideology provide understanding and interpretation of Islamic juristic principles which govern the boundary conditions of the legal framework as well as determine the scope and way of administration of Islamic social finance institutions.

#### 1.5.4. Data Collection Methods

These stakeholders were engaged in the research through interviews, focus group meetings, roundtable discussions and surveys through structured questionnaire. The data obtained was used to analyze the constraints in legal framework, obstacles in governance and administration and challenges at the institutional and operational level in execution. Different policy options were tabled and deliberated upon and refined through expert feedback from among the key stakeholders.

In order to provide concrete and informed policy advice, the existing regulatory framework, current governance and administration mechanism, past record of institutional delivery and past recommendations given by the Council of Islamic Ideology and other policy forums were analyzed through desk research of relevant extant literature and legal and policy documents.

To make the policy recommendations well informed regarding international best practices, the research team visited Malaysia to extensively understand their system of social finance. Figure 3 gives a snapshot of different tools of data collection that were employed in the study.

**Figure 3: Data Collection Methods**

#### 1.5.5. Methods of Data Analysis

The data and information gathered through these methods is further analyzed among research team and working group members to consolidate key learning points. First, the problems and obstacles in legal framework were identified. Then, the problems and obstacles in governance and administration were identified. In the light of these key learning points, policy steps were developed and discussed. The policy steps on which broad consensus was developed and which have a precedent in usage in global context were shortlisted further. Chapters 6 and 7 of the report present the policy steps.

In estimating potential of Zakat collection in Pakistan, micro-economic and macro-economic indicators were used. For this purpose, various mathematical values were summed, averaged and extrapolated to come up with potential aggregate collection in Pakistan.

In facilitating Zakat assessment, Zakat calculator was developed by using electronic spreadsheet. Different mathematical functions, statistical formulas and logical functions were used to facilitate smart inputs and calculations.

The empirical data on Zakat collection and disbursement, where available, was analyzed through descriptive statistical tools, such as measures of central tendency, measures of dispersion, frequency distribution tables, charts and graphs.



## Chapter 2

# Introduction to Islamic Social Finance in Pakistan

### 2.1. Market-Based Islamic Social Finance Institutions

Market-based Islamic social finance institutions include Takaful and Islamic microfinance. Social finance institutions are financial intermediaries that are not solely motivated and driven by profits. They have a social aim as well to enhance coverage of financial services and assistance to a broader cross section of people.

However, being market-based means that their services are not going to be free. Hence, their coverage will be limited by criterion of price. Two major institutions that fall under this category are Takaful and Islamic microfinance.

#### 2.1.1. Takaful: Concept and Structures

The Islamic alternative to conventional insurance is Takaful. It is based on mutual cooperation and joint responsibility. Cooperative insurance (Takaful) is permissible and is consistent with Shari'ah principles. Takaful provides risk protection in accordance with Shari'ah based on the principles of *Ta'awun* (mutual assistance).

The premiums paid in Takaful are unilateral payments on the basis of *Tabarru* (donation). This makes the relationship different from a bilateral monetary exchange where the payments from both parties are stipulated.

Operationally, Takaful refers to participants mutually contributing to the same fund with the purpose of having mutual indemnity in the case of peril or loss. Unlike insurance companies, whose investment income may contain Riba, Takaful companies invest funds in property, Islamic investment schemes, Shari'ah-compliant stocks and other Shari'ah approved securities like Sukuk.

Takaful also aims to provide compensation against possible losses, yet the crucial difference lies in the way this is done. In Takaful, not only the element of Riba (interest), Maysir (gambling) and Gharar (uncertainty) are avoided, but it is also ensured that all other Islamic principles are complied with. It is ensured through a Shari'ah supervisory board at the level of each Takaful company.

### 2.1.1.1. Takaful Products

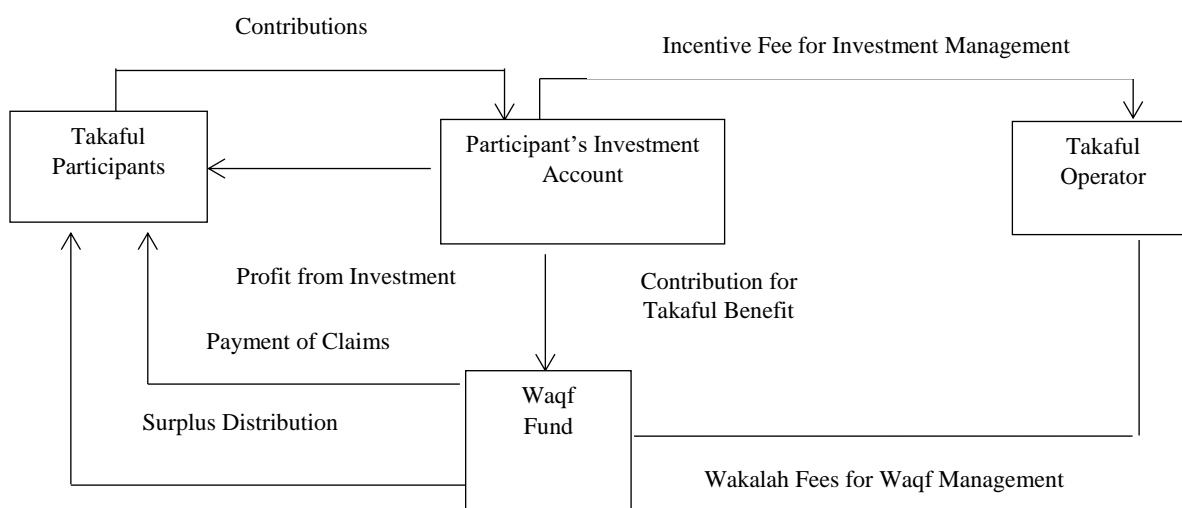
There are two major types of Takaful products. General Takaful plans are intended to meet the insurance needs of people and corporate bodies in connection with materialistic loss or damage due to any catastrophic condition.

Family Takaful plans are intended for broader needs which include long-term saving plans for meeting future financial needs, such as marriage, educational needs and health needs, for instance.

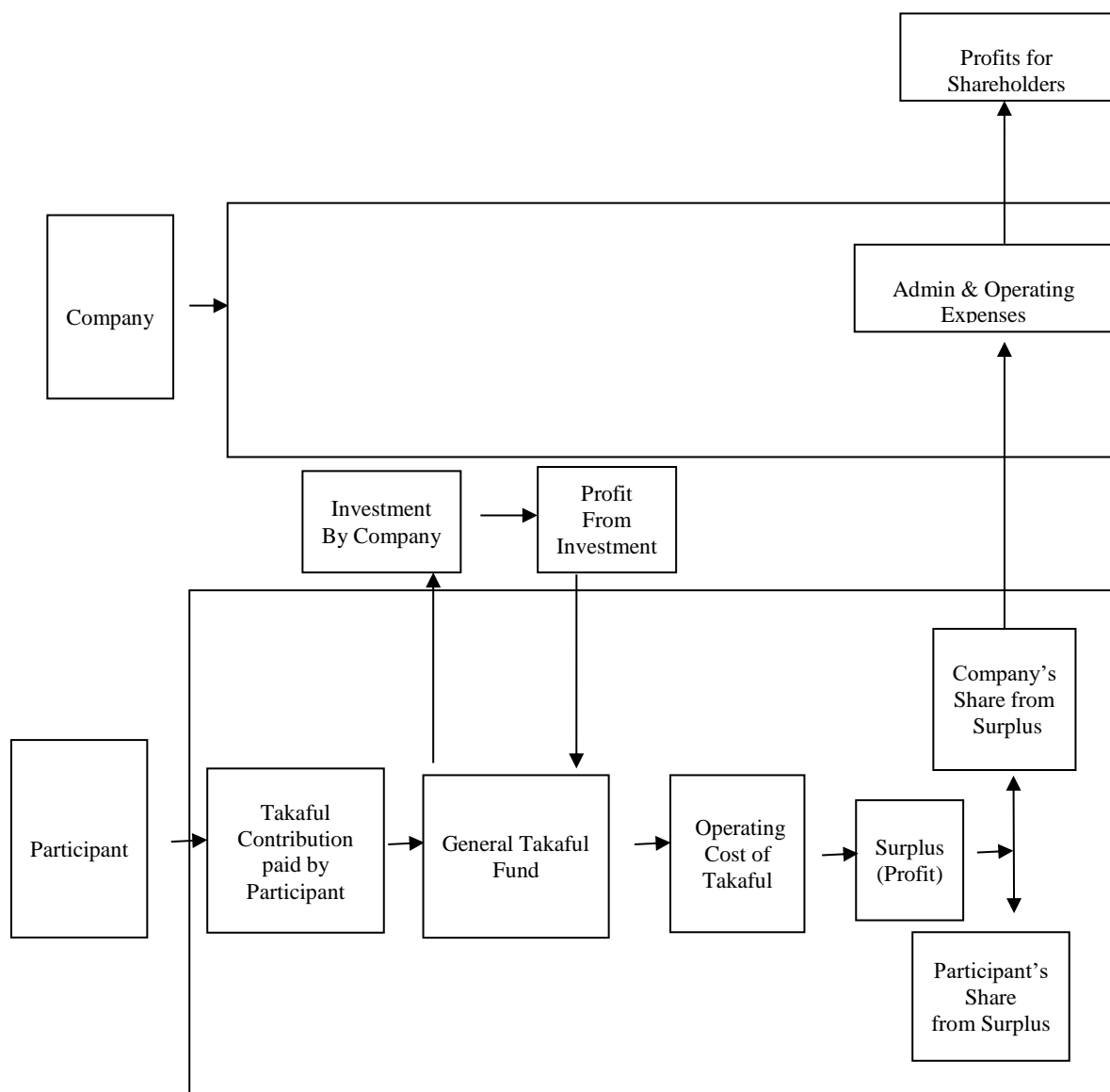
### 2.1.1.2. Takaful Models in Practice

**The Waqf-Wakalah Model:** In the Waqf model, the Takaful operator acts only as the Wakeel of the Waqf fund. If, at the end of the year, there is a surplus in the fund (i.e. after adding all its income and deducting all the payments), such surplus will be distributed amongst the participants proportionately after taking into account any claim benefits already availed. Cooperative risk sharing occurs among participants where a Takaful operator earns a fee for services (as a Wakeel or agent). Any surplus or deficit goes to the participants. Under the Wakalah model, the operator may also charge a fund management fee and performance incentive fee. A typical Wakalah-based Takaful model is illustrated in Figure 4.

**Figure 4: Takaful Wakalah Model**



**The Mudarabah Model:** Under the Mudarabah model, surplus (or profits) is shared fairly and equitably between the shareholders and the policyholders (i.e. the ‘participants’). On the other hand, under the Wakalah model, the surplus is returned entirely to the participants. Figure 5 describes the structure of Takaful Mudarabah model.

**Figure 5: Takaful Mudarabah Model**

Takaful sector in Pakistan is very small. Due to the high risk, low documentation, low savings rate and low asset ownership, insurance penetration in Pakistan is less than 1% of GDP. Micro-Takaful sector is even smaller. As per Pakistan Microfinance Network, there are only slightly over eight million policyholders in micro-insurance sector. However, many of them have limited coverage of insurance against sudden death only from the microfinance institutions.

The Government of Pakistan and provincial governments launched National Health Card scheme which provides health coverage to every citizen. However, the government has engaged State Life Insurance Corporation and its conventional insurance sector to provide the facility.

Health Takaful, Livestock Takaful and Crop Takaful are important services for farmers, but their coverage is very limited. It is estimated that around a million animals have lost their lives in floods in Pakistan in 2022 alone.

Salaam Takaful has a scheme of Livestock Takaful. It provides coverage against death due to:

- ❖ Fire
- ❖ Flood
- ❖ Risk of Calving
- ❖ Snake Bite
- ❖ Tornado and Cyclone
- ❖ Lightning and Electrocution
- ❖ Diseases
- ❖ Theft
- ❖ Loss of Udders/Teats due to any disease

Alfalah Insurance also provides Crop Takaful against natural calamities like excessive rains, hailstorm, frost, flood, drought, etc. The coverage also includes crop-related diseases like viral and bacterial attack, locust attack, etc.

Nonetheless, given that 40% of the labor force is engaged in agriculture, the coverage of these services is very limited and is only available on commercial basis. When natural calamities strike poor farmers, they have very little adaptive social protection coverage. The government's routine programs are also facing shortfall of funds. Hence, it becomes handicapped in providing adaptive social protection.

### 2.1.2. Islamic Microfinance

In Pakistan, approximately over one-third people suffer from multi-dimensional poverty as per UNDP report for Pakistan on multi-dimensional poverty. The headcount ratio (H) of multidimensional poverty is 38.8%. There may be more than 70 million poor people in Pakistan. As per Pakistan Microfinance Network, the number of active microfinance borrowers is around 8.5 million people. The average loan size is Rs. 25,000. But these loans are given at a price. The price of micro-credit may turn out to be higher than the lending rates of banks.

However, banks do not cater to micro borrowers. In fact, they do not even cater to Small and Medium Enterprises (SMEs) too much. Only 7% of total financing provided by banks goes to SMEs, as per State Bank of Pakistan. For Islamic banking, this ratio is even lower than 3% as per Islamic Banking Bulletin for June 2022 published by Islamic Banking Department of State Bank of Pakistan.

Thus, for those financially excluded poor people who wish to avoid Riba, Islamic microfinance is the only option to get microfinance since these poor people want to avoid bank interest as well as conventional microcredit services which are also interest-based.

Islamic microfinance is also a solution for involuntary financially excluded poor people who are considered as non-bankable by banks due to one of the following reasons:

- ❖ No stable income source.
- ❖ No verifiable source of income.
- ❖ No documentation in commerce and business.
- ❖ No legal registration of business.
- ❖ No financial or tangible assets which can be taken as collateral.
- ❖ Cost of administering small credit at individual level is not deemed as profitable by the banks.

Islamic microfinance is the only option for those financially excluded poor people who want to avoid Riba at any cost and do not get financing from interest-based banks or through conventional microcredit scheme.

#### 2.1.2.1. Microfinance Models

There are two broad categories of Islamic microfinance models that are globally used, i.e. charity based not-for-profit models and market-based commercial models.

The former model uses Qard al-Hasan for micro-credit and funds itself from charitable funds and government grants. Akhuwat is the largest non-interest based Islamic microfinance institution not only in the country, but arguably in the world.

Market-based commercial models provide micro-credit using Murabaha and micro-leasing using Ijarah. Murabaha financing is a way to finance assets and raw materials for deferred payment purchase. The poor client agrees to buy the asset from the Islamic micro-financial institution. Upon receiving this undertaking, Islamic micro-financial institution purchases the asset and subsequently sells it to the client at a profit. The client usually pays the deferred price in instalments or in one go after some period. Deferment of payment allows the client to benefit from the productivity and use of the asset to generate revenues without having the commitment to pay in the short term.

Ijarah allows financing of tangible fixed assets which are rentable. Islamic micro-financial institution buys the asset and provides it on lease basis to the client. The client uses the asset during the lease period and pays rent for the use of assets. After the lease term is over, the client purchases the asset from the Islamic micro-financial institution and becomes the sole owner.

## 2.2. Non-Market Based Islamic Social Finance Institutions

Non-market based Islamic social finance institutions include Zakat and Waqf in particular. Besides that, voluntary charity given as Sadqa also provides a source of assistance to the poor people. However, Zakat and Waqf are two most important institutionalized instruments of Islamic social finance for which the legal framework and administration also exists.

### 2.2.1. Zakat and Ushr

In the Islamic faith, Muslims are obliged to pay Zakat on surplus wealth and particular types of production. The rate of Zakat varies with the nature of assets and production process.

A 2.5% wealth Zakat is levied on currency, receivables, financial investments, provident fund, annuities, gold, silver, livestock and all assets held for trade. Zakat is exempted on wealth below Nisab and the assets in regular personal use like home, personal transport and furniture.

Nisab is threshold value of wealth below which Zakat is not obligatory. Since there was bi-metallic standard at the time of Prophet Muhammad (PBUH), Nisab was mentioned in both gold and silver. The cross over rate has changed overtime between gold and silver, and has a significant difference nowadays. Gold Nisab is almost nine times as much as silver Nisab in value. Some countries –Malaysia, Brunei, and Indonesia, for instance – follow the gold value of Nisab while some others use the silver value such as in Pakistan, India, Bangladesh, Afghanistan, etc. On livestock, the Nisab is different based on the count of livestock.

According to the mainstream Islamic jurisprudence of Ahl-e-Sunnat, wealth subject to Zakat would include:

- ❖ Gold, silver and other precious stones and metals held for trade
- ❖ Livestock including goats, cows, camels, sheep, etc.
- ❖ Stock-in-trade which is purchased for the purpose of sale
- ❖ Legal currency in the form of notes and coins
- ❖ Receivables which are expected to be received
- ❖ Financial investments, such as:
  - Equity investments
  - Investment in fixed income securities, such as bonds, debentures, Sukuk, etc.
  - Bank investments and money held in bank deposits
  - Investments in mutual funds
  - Life savings plans, annuities, fixed deposits, etc.

The ruling for tax on production value is based on the fact that there was a production value tax of 10% (Ushr) on the value of production from rain-fed lands. On the other hand, there was a production value tax of 5% on the value of production from irrigated lands. In essence, the irrigated lands had to be provided with the capital in the form of water supply.

The proceeds of Zakat and Ushr are to be spent on eight heads mentioned in the Qur'an.

“The alms are meant only for the poor and the needy, and those who are in charge thereof, those whose hearts are to be reconciled, and to free those in bondage, and to help those

burdened with debt, and for expenditure in the way of Allah, and for the wayfarer. This is an obligation from Allah. Allah is All-knowing, All-wise.” (Al Tawbah; V: 60)

These eight heads include:

- ❖ Poor with no assets and insufficient income. *Al-Fuqara*
- ❖ Poor with insufficient income. *Al-Masakin*
- ❖ Workers working on administration of Zakat. *Al-Amilin*
- ❖ New Muslim converts. *Muallafat al-Qulub*
- ❖ People in bondage. *Al-Riqab*
- ❖ People under debt. *Al-Gharimin*
- ❖ In way of Allah. *Fi Sibilillah*
- ❖ People as travelers. *Ibn al-Sabil*

The eight heads of Zakat mentioned in the Qur'an include:

- The needy
- The destitute
- Administrators of Zakat
- New Muslim converts
- Slave liberation
- Debtors
- Travelers

### 2.2.2. Waqf

The institution of Waqf implies holding or setting aside certain physical assets by the donor (Waqif) and preserving it so that benefits continuously flow to a specified group of beneficiaries or community.

A Cash Waqf is “the confinement of an amount of money by a founder(s) and the dedication of its usufruct in perpetuity to the welfare of society”.

The nature of the expected benefit or purpose of the Waqf is clearly stated in the Waqf deed or document created for this purpose by the Waqif. A traditional example of Waqf is that of donating or setting aside land for construction of a Masjid or a school or a hospital. The donor also specifies the trustee-manager(s) who would ensure that the intended benefits materialize and flow to the community. The trustee-manager is described as Mutawalli or Nazir.

Waqf is an important institution in Islamic social finance. It is similar to endowments. Under Waqf, an owner donates and dedicates an asset (movable or immovable) for the permanent societal benefit. The beneficiaries enjoy its usufruct and/or income perpetually.

In Muslim history, Auqaf (pl. of Waqf) provided public utilities (roads, water, and sewerage), educational institutions and hospitals. Even in contemporary times, Auqaf can also directly affect entitlements by providing educational scholarships and health services for the poor. Hence, the institution of Waqf can help in capacity building and wealth creation through building human, physical and financial capital.

In the contemporary application of Waqf, it can be established by dedicating real estate, furniture, other movable assets and liquid forms of money and wealth like cash and shares. The

Cash Waqf is usually formed where the pooled donations are used to build institutions, such as schools, hospitals, and orphanages. Cash Waqf can pool more resources and ensure wider participation of individual donors. The permissibility of making Waqf with contemporary forms of wealth like cash and shares increases flexibility and widens participation.

While Zakat can only be used for the eight specific categories of recipients mentioned in the Qur'an, Waqf offers flexibility in utilization of funds and can provide welfare services to both Muslims and non-Muslims.

One of the important features of Waqf is that it provides flexibility in fund utilization as compared to Zakat (almsgiving). Zakat funds must be utilized for specific categories of recipients as mentioned above.

On the other hand, the institution of Waqf can be used to provide a wide range of welfare services to Muslims as well as non-Muslims, and the beneficiaries could also be other living beings. For instance, animal protection programs and environmental preservation expenditures can be provided more flexibly through Waqf. In adaptive social protection, Waqf is a more flexible institution with which not only operating cost of programs, but fixed cost of infrastructure can also be financed.

The institution of Waqf can transform social capital into social and public infrastructure. It provides a permanent social safety net in the case of perpetual Waqf to the beneficiaries.

As compared to individual charity, the institution of Waqf is more effective in matching the right targets with objective screening and providing sustainable sources of funds to the beneficiaries. In individual charity, rich people often face difficulty in finding the right targets because their extended families and social circle normally comprise people like themselves.

Besides income support and cash transfers, poor people need training, capacity building and skills improvement in order to get out of poverty and achieve social mobility. It is often contented that lack of finance and business training requires institutional support to unleash the potentials of micro-entrepreneurs and to establish viable micro-enterprises.

Growth-oriented micro-finance programs also need to provide training, insurance, and skills enhancement facilities. In this regard, the institution of Waqf can improve the chances of socio-economic mobility by providing a rather permanent, effective and efficient funding source for the health and education infrastructure. The increased and improved provision of education and health infrastructure funded through Waqf can enhance the income earning potential of beneficiaries.

It is important to utilize the institution of Waqf and Zakat for capacity building of the poor so that they can build skills for income generation and subsequently become marketable clients for microfinance. The Waqf model can be used to fund the establishment of training and business support centers. Such non-credit services are essential for enhancing the skills and productivity of workers which can subsequently enhance their chances of gainful employment and achievement of socio-economic mobility.



Historically, in many Muslim societies, Waqf-based institutions were the sole providers (with no state intervention) of education, healthcare, water resources, and support for the poor. The list of social services even included the welfare of animals. The institution of Waqf, by creating community assets, has the potential to create robust sustainable institutions that may address educational, healthcare and other social needs in Muslim societies. Thus, Waqf is a viable, sustainable funding option for socially beneficial projects, thereby reducing dependency on public funds.

#### 2.2.2.1. Waqf in Pakistan

Currently, the Waqf system in Pakistan is largely passive. It aims to safeguard and maintain Waqf properties, such as mosques, shrines, and religious schools. Private or Corporate Waqf are not common. There is just one example of Corporate Waqf, i.e. Hamdard Laboratories. Among the four provinces, Punjab has a relatively more professionally run active department which carries out the following activities:

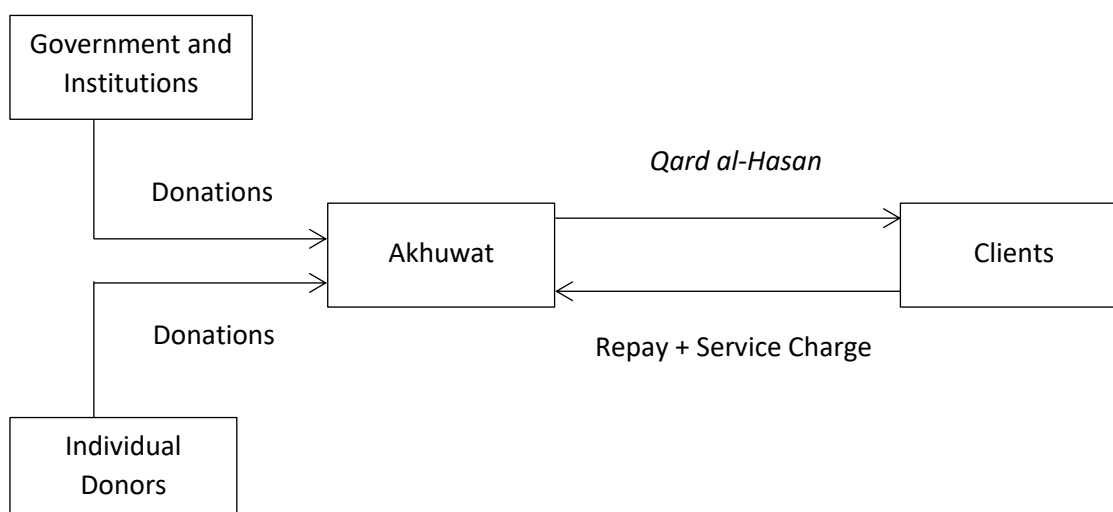
- ❖ Entering in leasing contracts based on tender offers from time to time.
- ❖ Investing funds in return generating investments with lower risk.
- ❖ Safeguarding and maintaining Waqf properties, especially those where visitors come often, such as shrines and historical mosques.
- ❖ Giving cash collection space on contract basis at frequently visited shrines.
- ❖ Building, renovation and maintenance work on Waqf properties.

However, currently, the institution of Waqf is not utilized for social protection or for development purposes. Legal framework does not provide role of Cash Waqf, Family Waqf and Corporate Waqf yet. The private sector, too, is unwilling to operate Waqf due to more legal flexibility in trust model and since property goes to government in Waqf. People having lack of trust in government prefer mutual help either through the mechanism of trust, society or association or they do it without formal legal institutionalization.

### Appendix 2.1: Case Study of Akhuwat

Akhuwat sources donations from individual and institutional donors and then provides Qard al-Hasan (interest free loans) to the clients. In turn, the clients agree to pay back the Qard (loan) amount at a stipulated time in future. For documentation, administration and screening of the applications, a nominal fixed amount is charged which is not a function of the amount of the loan.

Akhuwat had humble beginnings. Dr. Amjad Saqib, the founder of Akhuwat, started with a meagre donation given on individual basis. Then, it flourished into one of the largest microfinance institutions in the world. It now has more than 800 branches across Pakistan with 5.4 million beneficiaries. It has provided interest free loans of Rs. 180 billion. Through its more than 301 schools, it is providing education to around 50,000 students. Figure 6 illustrates Akhuwat's Qard al-Hasan model.

**Figure 6: Akhuwat Interest-Free Loan Microfinance Program**

Each Akhuwat branch has three employees: two loan officers and one branch manager. Every branch has permanent staff and there are also volunteers in the head office. The furniture and work design in the branch is kept simple to reduce cost and comfort the clients that the staff and branch are accessible to them. The staff sits on the floor with minimal stationary and required stamps, ledger and receipts.

Akhuwat is open to all. It provides interest-free microcredit to Muslims as well as non-Muslims. It does not discriminate between men and women and provides loan to a family unit.

#### *Time Duration from Application to Loan Disbursement*

Time duration from application to loan disbursement is one month. If one comes individually, two other persons should give guarantee of that person and these two persons will not be able to receive loan. If they apply while being guarantor of someone for another loan, then their application will be rejected. They will not be eligible to receive Akhuwat loan for 12 to 15 months.

As an alternative, Akhuwat suggests individual loan applicants to find two other persons who need money for business. If one is unable to return the amount, then the group will be responsible. The members should not be involved in any crime or drugs. The group member should not be relative of another member and their businesses should be different.

Borrowers are not forced to pay additional donation beyond the principal repayment. Akhuwat just recommends, but it does not force them. In practice, 20% do not pay and 80% pay additional donation. People give donations voluntarily. There is no fixed amount. Mostly people give donation from Rs. 10 to Rs. 100.

*Repeat of Loans*

Akhuwat keeps 10% of donation amount of first loan as a reserve every year and uses the remaining amount for Qard al-Hasan. This process continues until the loan amount reaches zero. For example, if Rs. 100 is donated to Akhuwat, it will keep Rs. 10 in reserve and lend Rs. 90 in the first year. In the second year, using Rs. 90, it will again keep Rs. 10 as a reserve and lend Rs. 80. Similarly, in the third year, it will keep Rs. 10 in reserve and lend Rs. 70. The process will continue till the tenth year where the lent amount will reach zero.

Loan to the same person can be given ten times. This kind of repeat loan has benefit as well as risk. The benefit is that it can help in achieving socio-economic mobility. The risk is that it may lead to habitual tendency to borrow. If a person repeats loan in dire circumstances, it may lead to further trouble. But, since Akhuwat does not charge any interest or mark-up, the benefit prevails over this potential risk. Emergency loans are also given, sometimes as quickly as within 30 minutes.

*Verification of Eligibility*

The loan officer makes a first visit to the applicant's home and judges his/her business and socio-economic status. After that, the branch manager visits again to determine the beneficiary's eligibility.

Branch staff checks the condition of the home of the beneficiary. For example, total number of family members, total dependent family members, total independent family members, last electricity bill paid, kitchen expenditures, medical bills, and mode of transportation used. On visiting the kitchen, loan officers judge their economic status and also make verifications from the neighbors.

*Loan Recovery*

Branch staff does office work in the first 10 days of the month and do loan recovery while at the branch. After the tenth day, the staff starts visiting the applicants' homes.

*Verification of Use of Loan after Disbursement*

Branch staff conduct inspection by visiting the home or business place after one week of fund disbursement to see whether the amount has been utilized for the stated purpose or not. However, Akhuwat believes in trust and dignity. It does not ask for slips. People can forge slips as well. Akhuwat wants to build and maintain trust with the beneficiaries so that they feel dignity and self-respect. This treatment encourages them to avoid misreporting and willful delay in repayment.

Akhuwat's activities are carried out in mosques. The spiritual link is also created so that people regard receipt of the loan as a gift from their Creator and comply with repayment obligations.

Success stories of socio-economic change at individual level are various. One branch manager apprised that in 2014, when he was at Data Sahab branch, a disabled person who did not have legs came there. He took Rs. 10,000 loan and later asked for a second loan of Rs. 40,000. He used this amount to purchase two press machines. He was living in a rented home and had seven daughters with no son. Now, he works with his daughters and has purchased his own house. He later established a factory and hired a number of employees.

Nonetheless, sometimes, there are cases of wrong information being provided. A woman said that she is a widow, but the branch manager found her husband when he visited her home.

#### *Amount of Loan*

The amount of loan varies across clients and people take money according to their need. Akhuwat gives a maximum loan of Rs. 200,000 for two years. For smaller loans, the repayment is between 12 to 15 months. There is a minimal fixed fee of Rs. 200 for documentation and processing.

#### *Repayment Schedule*

Previously, against a loan of Rs. 15,000, the instalment amount was Rs. 1,000, and against a loan of Rs. 20,000, the amount was Rs. 1,500. For a loan of Rs. 25,000, the Akhuwat instalment was Rs. 1,500 and for Rs. 30,000, it was Rs. 2,000. Now, for Rs. 15,000 and Rs. 20,000 loans, the beneficiaries are asked to pay an instalment of Rs. 2,000 per month.

#### *Disbursement Mode*

Earlier, cheques were used. Now the beneficiaries receive a message from Allied Bank after which they can get their funds from any branch of the bank.

Akhuwat carries out all activities through online platform. Even in Balochistan, it disburses funds online. Akhuwat receives 90% recovery in the office in the first 10 days of the month. If people are late, then the branch officer calls them and they send the instalment through someone.

#### *Funds Received from the Head Office*

A branch gets funds according to its needs. Sometimes, a branch receives less money than required. The branches also receive donations from the general public. After having received a donation, the branch staff sends them an online message about their donation.

#### *Response of Beneficiaries*

Upon visiting the 500th branch of Akhuwat, the research team of Institute of Policy Studies also met some beneficiaries at random. One beneficiary, Ms. Hina, informed that someone provided her information about Akhuwat. According to her, she came to the branch and found

the office staff very cooperative. She was a resident of Bhatti Gate, Lahore. She mentioned in her application that her husband is an electrician and she sews clothes to make ends meet. She wanted to expand the sewing business. For the first loan, she was given Rs. 35,000 and she returned it in one year. From the amount, her husband used some money for his work and she used some of it for purchasing sewing material. Now, she is applying for Rs. 50,000 loan.

#### *Transgender Project*

Akhuwat gives Rs. 25,000 as a stipend to transgenders. Moreover, Akhuwat is now working on a project whose objective is educating the transgender community. For that, it is building schools where the transgender persons will be provided free education up to higher secondary schooling and then technical skills education. Furthermore, the transgenders who want to pursue higher education will be encouraged to become doctors, engineers, etc.

#### *Obstacles Faced by Akhuwat*

The government does auditing every now and then and asks about details of personal assets of the executives. Court litigations also take away a lot of time and resources from core activities.

Even though the program has no cost to the customer, but some of the projects rest on donations and support of government. Since Zakat is not allowed for Qard al-Hasan by scholars in Pakistan, people cannot give their Zakat to Akhuwat. Since charitable payments other than Zakat are voluntary under both the law of the land and the law of Allah, crowdfunding is not that stable without Zakat funds.

## Chapter 3

# Legal Framework and Outreach of Islamic Social Finance

### 3.1. Legal Framework of Islamic Social Finance in Pakistan

#### 3.1.1. Zakat and Ushr Acts in Provinces

In KP, Zakat and Ushr Act, 2011 governs the Zakat and Ushr administration. In the other provinces, there are different acts, such as:

- ❖ Punjab Zakat and Ushr Act, 2018
- ❖ Sindh Zakat and Ushr Act, 2011
- ❖ Balochistan Zakat and Ushr Act, 2012

These acts take almost all their inspiration from the Zakat and Ushr Ordinance, 1980. After the 18th Amendment in the 1973 Constitution of Pakistan, devolution of authority took place from the federal government to the provinces in many subjects including social protection. After that, each province came up with a separate legislation of its own to manage Zakat and Ushr administration.

However, the details of the acts are nearly the same as Zakat and Ushr Ordinance, 1980. The only major change is that now the top most authority is the provincial chief Zakat administrator rather than some representative of the federal government.

#### *Zakat Charge and Collection*

Section 3 (a) of Zakat and Ushr Act, 2011 in KP province gives the right to get exemption from Zakat payment to almost every person. This clause has made the Zakat system highly decentralized with people submitting affidavit to the deducting agency, such as bank or brokerage house, to claim exemption from compulsory Zakat deduction. Section 3 (a) stipulates:

*“No Zakat or Ushr shall be charged or collected on compulsory basis in respect of the assets or the produce of a person who, not less than thirty days preceding the valuation date in the case of Zakat, and at any time before the valuation date in the case of Ushr, files with the deducting agency, or with the Local Committee in the case of Ushr, a declaration, or an attested copy thereof, in the prescribed form, sworn by him before a Magistrate, an oath*

*Commissioner, a notary public, or any other person authorized to administer oath in the presence of two witnesses who identify him, to the effect that he is a Muslim and a follower of one of the recognized Fiqhs, which he shall specify in the declaration, and that his faith and the said Fiqh do not oblige him to pay the whole or any part of Zakat or Ushr in the manner laid down in this Act.”*

The law also allows refund to such a person if he does not wish to leave it in the Zakat funds as Sadqa or Khairat in the name of Allah as a manifestation of the unity of the Ummah and claims refund.

#### *Compulsory vs Non-Compulsory Heads of Zakat*

The law mentions Zakatable assets and production forms on which Ushr is levied in the First and Second Schedule of the Zakat and Ushr Act, 2011. The First Schedule includes assets on which Zakat will be deducted at source by a deducting agency.

The deducting agency could be a bank which would deduct compulsory Zakat on saving accounts held by Muslim citizens in Pakistan. The deducting agency could be an investment broker managing the trading on behalf of investors. Zakat is also applied on dividend income.

The First Schedule mainly mentions financial assets and wealth forms, such as:

- ❖ Saving accounts at banks, post offices, National Savings Centers and other financial institutions keeping such accounts.
- ❖ Notice deposit receipts and accounts and similar receipts at banks, post offices, National Savings Centers and other financial institutions issuing such receipts and keeping such accounts.
- ❖ Fixed deposit receipts and accounts and similar receipts and accounts and certificates (e.g. Khas Deposit Certificates) issued by banks, post offices, National Savings Centers and financial institutions, on which return is receivable by the holder periodically or is received earlier than maturity or withdrawal.
- ❖ Savings/deposit certificates (e.g. Defence Savings Certificates, National Deposit Certificates).
- ❖ Units of the mutual fund, such as National Investment (Unit) Trust.
- ❖ Government securities on which return is receivable by the holder periodically.
- ❖ Securities including shares and debentures of companies or statutory corporations (excluding those held in the name of a company or a statutory corporation), on which return is payable periodically or otherwise, and is paid.
- ❖ Annuities.
- ❖ Life insurance policies.
- ❖ Provident funds.

The Second Schedule also mentions all other asset forms on which Zakat is due in personal capacity, but government would not deduct Zakat on them compulsorily.

The Second Schedule mentions financial assets, wealth forms and production type:

- ❖ Gold and silver and manufacturers thereof.
- ❖ Cash.
- ❖ Prize bonds.
- ❖ Current accounts and foreign currency accounts.
- ❖ Loans receivable excepting loans receivable by banks, other financial institutions, statutory corporations and companies.
- ❖ Securities including shares and debentures, to the extent not subject to compulsory levy of Zakat under the First Schedule.
- ❖ Stock-in-trade of:
  - Commercial undertakings including dealers in real estate.
  - Industrial undertaking.
  - Precious metals and stones and manufacturers thereof.
- ❖ Agricultural including horticultural and forest produce
  - Tenant share.
  - Other than tenant's share.
- ❖ Animal (fed free in pastures)
  - Sheep or goat.
  - Bovine animals.
  - Camels.
- ❖ Wealth and financial assets other than those listed in First and Second Schedule on which Zakat is payable according to Shari'ah.

#### *Secrecy of Information*

Section 4 of Zakat and Ushr Act, 2011 for KP ensures that any information furnished or collected in connection with the deduction of Zakat at source under this Act shall be treated as secret and shall not be used for any other purpose, including the assessment or collection of any tax.

Section 4 of Zakat and Ushr Act, 2011 for KP ensures that any information furnished or collected in connection with the deduction of Zakat at source under this Act shall be treated as secret and shall not be used for any other purpose, including the assessment or collection of any tax.



*Charge and Collection of Ushr*

Section 5 stipulates that Ushr is applied on the produce of every landowner, allottee, lessee, lease-holder or land-holder at the rate of 5% of his share of the produce.

However, it gives the provision that if any plot of land is used principally for growing one crop and a small portion thereof, not exceeding one-fourth of an acre, is used for growing another crop, Ushr shall not be charged in respect of the produce of such small portion.

The Act limits the Nisab to five Wasaq, i.e. 948 kilograms of wheat, or its equivalent in value in the case of other crops liable to Ushr. The Act also clarifies that Ushr shall be the first charge on the produce and Ushr shall be collected in cash. However, it allows that where the produce consists of wheat or paddy, Ushr at the option of the Zakat and Ushr Council may be collected in kind.

In the mode of assessment of Ushr, the Act mentions that in the case of lease, the liability of the lessor and lessee to pay Ushr shall be equitably apportioned between them by the Tehsildar.

*Establishment of Zakat Funds*

The Zakat and Ushr Act, 2011 for KP requires that the following Zakat funds shall be established, namely:

*Provincial Zakat Fund*

In the Provincial Zakat Fund, the following shall be credited:

- ❖ Zakat deducted at source.
- ❖ Zakat paid into it voluntarily including voluntary contribution made by Pakistani citizens and other persons residing abroad.
- ❖ Transfers, if any, from the District Zakat Funds; and grants, atiyat and any other receipts including voluntary contributions made by Pakistani citizens and other persons residing abroad.
- ❖ Transfer of funds, if any, from the federal government.

*District Zakat Fund*

In District Zakat Fund, the following shall be credited:

- ❖ Transfers to it from the Provincial Zakat Fund.
- ❖ Zakat paid into it voluntarily.
- ❖ Transfers, if any, from the Local Zakat Funds.
- ❖ Grants, atiyat and any other receipts.

*Local Zakat Fund*

In Local Zakat Fund, the following shall be credited:

- ❖ Zakat paid into it voluntarily.
- ❖ Transfers to it from the District Zakat Fund.
- ❖ Transfer to it from the Provincial Zakat Fund.
- ❖ Grants, atiyat and any other receipts.

*Utilization of Zakat Funds*

Section 8 of the Zakat and Ushr Act, 2011 for KP mentions that the money in a Zakat fund shall be utilized for the following.

- ❖ Needy, indigent, poor (particularly orphans and widows), handicapped and disabled.
- ❖ Affected (needy) persons from natural calamities.
- ❖ Expenditure on collection, disbursement, and administration of Zakat and Ushr (capped at 10% of the total Zakat collection amount). If expenditure on the administrative organization of a District Zakat and Ushr Committee is not fully met by the government, the Council may provide supplementary funds not exceeding 2%.
- ❖ Investment in any non-interest bearing instruments permitted under Shari'ah.
- ❖ Any other purpose permitted by Shari'ah.

*Disbursements from Zakat Funds*

Section 9 of the Zakat and Ushr Act, 2011 for KP mentions that the Council shall prepare budget for each financial year.

The Council may, from the Provincial Zakat Fund, make disbursements and transfer funds to the District Zakat Funds on the basis of population or to an institution in such form that help the needy and the poor.

A District Zakat and Ushr Committee may make disbursements and transfer funds through crossed cheques or bank advice, banks, post offices or any other financial institutions from District Zakat Fund to the eligible persons or to a Local Zakat Fund or to any other institution or incur other administrative expenditure.

A Local Zakat and Ushr Committee shall make disbursement or incur expenditure from the Local Zakat Fund through crossed cheques in the prescribed manner.

A Local Zakat and Ushr Committee may, if required by the Council or the District Zakat and Ushr Committee, transfer any funds surplus for its needs from the Local Zakat Fund to the Provincial Zakat Fund or, as the case may be, the District Zakat Fund.

The Council or a District Zakat and Ushr Committee shall disburse Zakat through a bank or a post office or any other financial institution as may be determined by the Council.

#### *Accounts and Audit*

Section 10 in Zakat and Ushr Act, 2011 for KP specifies that the accounts of the Central Zakat Fund, a Provincial Zakat Fund, a District Zakat Fund, and a Local Zakat Fund shall be maintained and operated, respectively, by the Administrator-General, the Chief Administrator, the District Committee and the Local Committee, in such form and manner as may be prescribed.

Section 11 of the Zakat and Ushr Act, 2011 for KP stipulates that to carry out audit of the Provincial Zakat Fund annually or at shorter intervals, the Zakat and Ushr Council shall request the Auditor General of Pakistan to conduct the audit. To carry out audit of a District Zakat Fund annually or at shorter intervals, the Zakat and Ushr Council shall request the Auditor General of Pakistan to conduct the audit. To carry out audit of the Local Zakat Funds within a district annually or at shorter intervals, the District Committee shall request the Auditor General of Pakistan to conduct audit of the Local Zakat Fund. The audit performed by the Auditor General of Pakistan shall include propriety audit.

#### *Organization and Administration of Zakat*

Sections 12 through 15 of the Zakat and Ushr, 2011 for KP provides details on the organization and administration of Zakat in the province. It is indicated that the government shall establish the Khyber Pakhtunkhwa Zakat and Ushr Council to exercise general superintendence and control over matters relating to Zakat and Ushr, particularly the Zakat funds in the province and the maintenance of their accounts in the prescribed manner.

The hierarchy runs as follows: Chief Administrator, under whom are District Zakat and Ushr Committees and which supervise and work through Local Zakat and Ushr Committees.

#### *Chief Administrator*

The government shall appoint a Chief Administrator on such terms and conditions as may be determined by the government or the Secretary Zakat and Ushr Department will act as Chief Administrator.

#### *District Zakat and Ushr Committee*

In each district, a District Zakat and Ushr Committee, shall be constituted by Zakat and Ushr Council for the following functions: to oversee the functioning of administrative organization of Zakat and the assessment of Ushr and atiyat and the disbursement and utilization of the moneys in the District Zakat Fund and the Local Zakat Fund; and prepare and maintain accounts of the District Zakat Fund in such form and manner as may be prescribed.

*Local Zakat and Ushr Committee*

A Local Zakat and Ushr Committee shall be constituted for each: (a) revenue estate in settled rural area; (b) deh or village in non-settled rural area; and (c) ward in urban area.

**3.1.2. Legal Framework of Waqf in KP**

The Khyber Pakhtunkhwa Waqf Properties (Amendment) Act, 2020 governs the management of Waqf and Waqf properties in KP province.

*Definition of Waqf Property*

A Waqf property means property of any kind permanently dedicated by a person professing Islam for any purpose recognized by Islam as religious, pious or charitable, but does not include property of any Waqf such as is described in Section 3 of the Mussalman Waqf Validating Act, 1913 (VI of 1913), under which any benefit is for the time being claimable for himself by the person by whom the Waqf was created or by any member of his family or descendants.

The law further explains which properties shall be considered as Waqf properties.

- ❖ If a property has been used from time immemorial for any purpose recognized by Islam as religious, pious or charitable, then in spite of there being no evidence of express dedication, such property shall be deemed to be a Waqf property.
- ❖ Property allotted in lieu of or in exchange of Waqf property left in India shall be deemed to be Waqf property.
- ❖ Property of any kind acquired with the sale proceeds or in exchange of or from the income arising out of Waqf property or from subscription raised for any purpose recognized by Islam as religious, pious or charitable, shall be deemed to be Waqf property.
- ❖ The income from boxes placed at shrines and offerings, subscriptions or articles of any kind, description or use presented to a shrine or to any person at the premises of a shrine shall be deemed to be a Waqf property.
- ❖ Property permanently dedicated for the purposes of a mosque, Takia, Khankah, Dargah or other shrines shall be deemed to be a Waqf property.
- ❖ Relief for the poor and the orphans, education, workshop, medical relief, maintenance of shrines and the advancement of any other object of charitable, religious or pious nature or of general public utility shall be deemed to be charitable purposes.

*Appointment of Chief Administrator of Auqaf*

The government shall appoint a Chief Administrator of Auqaf for Khyber Pakhtunkhwa. He must be a Muslim and possess such qualifications as may be prescribed by the government. The government may, by order, vest in him, the Waqf properties situated in the province including all rights, assets, debts, liabilities and obligations relating thereto.

The government may appoint Deputy Administrators on such terms and conditions as may be prescribed or assign duties of the Deputy Administrator to the Assistant Commissioner (Headquarter) of each District for performance of the functions of Deputy Administrator.

#### *Registration of Waqf Property*

Any person or persons in charge of, or exercising control over the management of any Waqf property whether a creator of the Waqf or otherwise, or any authorized representative nominated by them, shall get such Waqf property registered with the Chief Administrator within ninety days of the creation of the Waqf.

#### *Reporting of Waqf Property*

The District Collector (Revenue), being the custodian of the land record and the Registrar (Revenue), being the focal point of registering all deeds, agreements and documents etc., shall furnish, in the prescribed manner, a consolidated annual report of all Waqf properties recorded as Waqf during the year in respect of their respective district to the Chief Administrator for information and further necessary action, as deemed appropriate by the Chief Administrator under the provisions of law for the time being in force. The law also requires that at the end of each financial year, the Chief Administrator shall prepare and submit report of the Waqf properties.

#### *Eviction of Persons Wrongfully in Possession of Waqf Properties*

If any person is in occupation of or enter upon, or is using any immovable Waqf property to the occupation or use of which he is not, or has ceased to be, entitled by virtue of any provision of this act, the Chief Administer or any other person authorized by him may, after giving such person a reasonable opportunity of showing cause against the action proposed to be taken, evict him forthwith from such property with use of such force as may be necessary.

If any building or other structure has been erected on any property while it was in the occupation or use of a person evicted therefrom shall stand forfeited to the Chief Administrator.

#### *Leasing Properties to Generate Income for Charitable Spending*

The Chief Administrator shall lease out the Waqf property for such period as may be prescribed and the income derived from such property shall be used for any purposes recognized by Islam as religious, pious or charitable as the Chief Administrator may deem fit.

#### *Sale of Waqf Property by Chief Administrator*

A Waqf property shall be used for the purpose for which it was dedicated or has been used or for any purpose recognized by Islam as religious, pious or charitable, as the Chief Administrator may deem fit. However, the government may, where it is satisfied that

circumstances exist in which it is necessary to sell or otherwise dispose of any Waqf property, may order the sale. The reasons could be:

- a) To secure maximum economic benefits out of such property and to avoid loss or damage to such property; or
- b) To serve the best public interest and public purpose for which such Waqf property was dedicated; or
- c) To enable the property to be used, in the absence of evidence of express dedication, for the purpose for which it has been used or for any purpose recognized by Islam as religious, pious or charitable; or
- d) To provide maintenance to those who, on account of unemployment, sickness, infirmity or old age are unable to maintain themselves; or
- e) To provide education, medical aid, housing, public facilities and services such as roads, sewerage, gas and electric power; or
- f) To prevent danger to life, property or public health.

#### *Managing Administration and Reporting*

The Chief Administrator shall maintain a complete record of all properties under his control and management, and shall keep accounts of income and expenditure of such properties. All moneys received or realized by the Chief Administrator in respect of properties under his control and management shall form and be credited to, a fund to be called Auqaf Fund. At the end of each financial year, the accounts maintained by the Chief Administrator shall be audited by such authority as may be prescribed and the Audit Report with the comments of the Chief Administrator shall be laid before the government.

Rent and lease money in respect of Waqf property may be recovered as arrears of land revenue. Any sum due as rent or lease money in respect of Waqf property, the administration whereof has been taken over and assumed by the Chief Administrator, if not paid within thirty days of it having become due, may be recovered as arrears of land revenue.

#### *Terminating a Lease on Breach of Conditions*

If the Administrator is satisfied that a lessee or tenant or any immovable Waqf property has committed a breach of the condition of lease or tenant, the authority may give a notice to appear before the authority and state his objections to an order being made for the termination of lease or resumption of the tenancy.

### **3.1.3. Legal Framework for Islamic Microfinance by Financial Institutions**

State Bank of Pakistan had prescribed guidelines aiming to provide enabling environment for introduction of microfinance products and services on Shari'ah compliant basis in the country through various channels.

*Provision for Offering Islamic Microfinance by Financial Institutions*

Islamic microfinance services and products can be offered by various types of financial institutions, in different forms, which are under following options.

*Option 1. Establishing Full-Fledged Islamic Microfinance Banks (IMFB)*

The company granted license to operate as Islamic MFB shall comply with the provisions of Microfinance Institutions Ordinance, 2001, rules/prudential regulations framed under it and SBP directives issued from time to time.

*Option 2. Islamic Microfinance Services by Full-Fledged Islamic Banks*

Full-fledged Islamic banks are allowed to use the same institutional arrangements allowed to commercial banks vide SMED Circular No. 10 dated June, 27, 2006, which include:

- ❖ Establishing IsMF counters in the existing branches,
- ❖ Opening of standalone IsMF branches,
- ❖ Establishing independent IsMF subsidiaries with independent and professional board and management,
- ❖ Developing linkages with MFBs licensed by SBP and NGO-MFIs that are not licensed by SBP to extend wholesale funds in a Shari'ah-compliant manner.

*Option 3. Islamic Microfinance Services by Conventional Banks*

Conventional banks which have been issued license for Islamic banking branches can offer Islamic microfinance products through following modes:

- ❖ Microfinance counters at existing branches
- ❖ Standalone Islamic microfinance branches and mobile banking
- ❖ Establishing independent Islamic MFBs as subsidiaries of conventional banks
- ❖ Developing linkages with Islamic MFBs/MFIs

*Option 4. Islamic Microfinance Services by Conventional Microfinance Banks*

Conventional MFBs are also allowed to offer Islamic microfinance products and services subject to the following conditions. Any MFB desirous of offering Islamic microfinance products and services shall be required to apply to the State Bank for permission to start Islamic microfinance.

The eligibility of a MFB to offer Islamic microfinance services shall be considered by the State Bank. Upon satisfaction, SBP shall grant an approval in principle to the bank for offering Islamic microfinance products and services upon such terms and conditions as it deems fit.

*Minimum Paid-up Capital Requirement*

The MFIs' legal framework allows establishment of three categories of formal microfinance banks in the country viz:

- ❖ Nationwide MFBs – minimum paid-up capital of Rs. 500 million.
- ❖ Province-wide MFBs – minimum paid-up capital of Rs. 250 million.
- ❖ District-wide MFBs – minimum paid-up capital of Rs. 100 million.

The sponsors granted NOC for incorporation of the proposed bank with Securities and Exchange Commission of Pakistan as public limited company, shall, after incorporation of the company, submit the incorporation certificate to SBP. The State Bank shall grant the license subject to receipt of clearance from security agencies and Federal Board of Revenue (FBR).

*Structure of the MFB Board*

The MFB Board shall have at least seven members and not more than 25% of the members shall be from the same family. No person shall be on the board of more than one microfinance bank/institution. Similarly, no group shall be granted license for establishing more than one microfinance bank/institution.

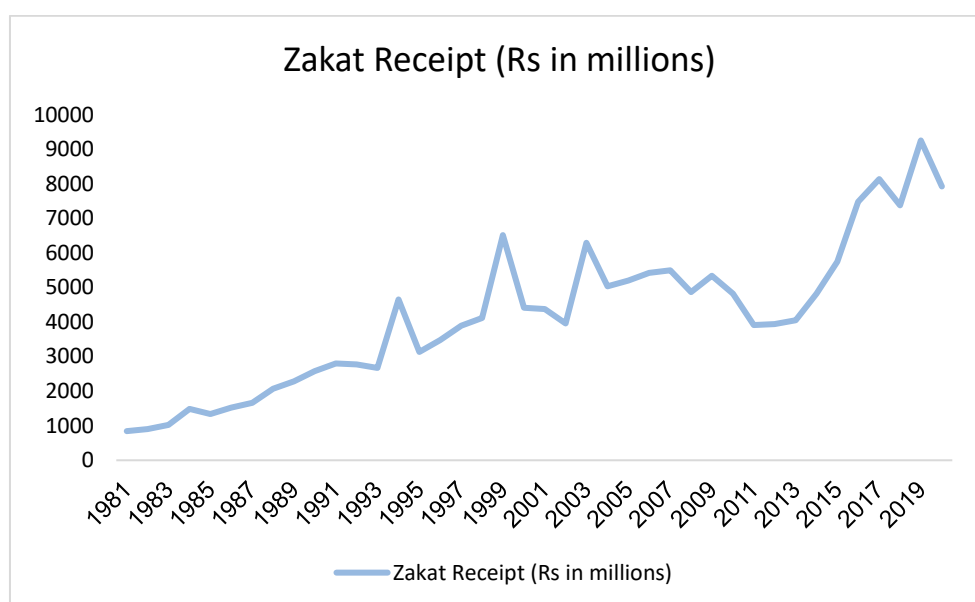
## 3.2. Footprint and Outreach of Islamic Social Finance in Pakistan

### 3.2.1. Current Collection of Zakat

Currently, the federal collection of Zakat receipts is meager. Almost complete reliance is on deduction of Zakat from bank accounts and financial income and wealth at source by deducting agency.

Voluntary collection is almost nonexistent. The provinces or even the federal government does not have any collection mechanism. There are no efforts being put in as well. With the declining level of trust among the general public with regards to transparency and strong governance and administration, the governments have also resigned to the fact that let the Zakat administration be passive and in private sphere. As little as a few billion rupees of Zakat is collected even after the financial inclusion and market capitalization of stock market has increased manifold in the last two decades.



**Figure 7: Zakat Receipts (in million rupees)**

**Source: Handbook of Pakistan Economy**

Figure 7 shows the trend of Zakat receipts overtime during the last four decades, starting from 1981. It can be seen that there is very slow growth even in absolute terms.

Table 1 shows the break-up of Zakat receipts for the year 2020. It can be seen that almost all Zakat is deducted at source. Even within the Zakat collection deducted at source, almost two-thirds comes from bank accounts, followed by government saving schemes, provident funds and life insurance policies.

**Table 1: Zakat Receipts on Different Items (2022)**

Items	(In mln Rs.)
Saving Bank Accounts and Similar Accounts	6,594
Notice Deposit Receipts and Accounts	392
Fixed Deposit Receipts and Accounts (Periodically)	896
Fixed Deposit Receipts and Accounts (on Maturity or Encashment)	506
NIT Units	29
Shares and Debentures of Companies	323
Annuities	4
Life Insurance Policies	390
Provident Credit Balances	1,522
Total Deduction of Zakat at Source	10,657
Zakat Voluntarily Paid	4
Other Receipts	158
Total Receipts	10,818

**Source: SBP Annual Report, 2022**

### 3.2.2. Outreach of Microfinance

As per Pakistan Microfinance Network, the number of active microfinance borrowers are around 8.5 million people. The average loan size is Rs. 25,000. Table 2 summarizes the outreach statistics of microfinance in Pakistan. The bifurcation of Islamic microfinance is not given. But, Pakistan Microfinance Network estimates that Islamic micro-financial services have a share of 10% to 15% in various segments.

**Table 2: Outreach Statistics of Microfinance**

Indicators of Microfinance	Figures for Q3 2022
Number of Branches/Units	4,094
Number of Districts Covered	139
Penetration Rate (%)	42.7
Active Borrowers	8,775,378
Gross Loan Portfolio (Rs. in millions)	470,137
Number of Loans Disbursed	5,611,258
Disbursements (Rs. in millions)	140,561
Average Loan Size (Rs.)	25,050

**Source: Pakistan Microfinance Network**

But, these loans are given at a price. Price of micro-credit may turn out to be higher than the lending rates of banks. It is because banks find it costlier to cover fixed cost of monitoring, documentation and staff deployment to administer and monitor microcredit to the micro borrowers. For instance, Apna Microfinance Bank charges 19% to 24% flat rate of interest. Khushhali Microfinance Bank has 34% rate of interest on its livestock loan.

Table 3 gives the breakup of microfinance penetration across provinces including the details of infrastructure, active borrowers and loan portfolio size.

**Table 3: Outreach of Microfinance**

Province/Region	Offices		Micro-Credit	
	Fixed	Mobile	Active Borrowers	Gross Loans (Rs.)
AJK	90	-	106,555	7,337,323,633
Balochistan	52	-	40,595	4,790,827,169
Gilgit-Baltistan	72	1	54,688	8,705,121,239
FATA	30	-	24,908	1,046,105,935
Islamabad	28	5	2,202,090	8,036,136,881
KP	232	14	202,579	22,555,143,433
Punjab	2,710	22	4,781,672	322,734,012,880
Sindh	838	-	1,362,291	94,932,545,499
Total	4,052	42	8,775,378	470,137,216,669

Some of the major microfinance banks in Pakistan include:

- ❖ Advans Pakistan Microfinance Bank
- ❖ APNA Microfinance Bank
- ❖ FINCA Microfinance Bank
- ❖ Khushhali Microfinance Bank
- ❖ Mobilink Microfinance Bank
- ❖ NRSP Microfinance Bank
- ❖ LOLC Microfinance Bank  
(Formerly Pak Oman Microfinance Bank)
- ❖ Sindh Microfinance Bank
- ❖ U Microfinance Bank
- ❖ Telenor Microfinance Bank
- ❖ ASA Pakistan
- ❖ HBL Microfinance Bank

Some of the major non-bank microfinance companies in Pakistan include:

- ❖ Agahe Pakistan
- ❖ Akhuwat Islamic Microfinance Company
- ❖ AMRDO Foundation
- ❖ Farmers Development Organization
- ❖ Badbaan Community Development Microfinance Company
- ❖ CSC Empowerment and Inclusion Programme
- ❖ Damen Support Programme
- ❖ FFO Support Program
- ❖ Islamic Relief Pakistan
- ❖ JWS Pakistan
- ❖ Kashf Foundation
- ❖ Micro Options Support Program
- ❖ Mojaz Support Program
- ❖ Naymet Trust
- ❖ Orangi Pilot Project
- ❖ OPD Support Program
- ❖ Orix Leasing Pakistan
- ❖ Pak Villagers Development Foundation
- ❖ SAATH Development Society
- ❖ SAFCO Microfinance Company

- ❖ Sayya Microfinance Company
- ❖ Shadab Rural Development Organization
- ❖ Shah Sachal Sami Foundation
- ❖ Soon Valley Development Program
- ❖ Sungi Development Foundation
- ❖ S.W.W.S
- ❖ Taleem Finance Company
- ❖ Thardeep Microfinance Foundation
- ❖ Wasil Foundation
- ❖ Union Microfinance

Then, there are also rural community development programs, such as:

- ❖ Ghazi Barotha Taraqiati Idara
- ❖ National Rural Support Programme
- ❖ Punjab Rural Support Programme
- ❖ Sarhad Rural Support Programme
- ❖ Sindh Rural Support Organization

### 3.2.2.1. Outreach of Microinsurance

When it comes to Takaful sector, it is majorly catering to the general Takaful and family Takaful needs of urban dwellers in upper middle and upper class households. Takaful operators are incorporated as profit oriented companies and they provide their services with a commercial motive while abiding by the stipulations of Shari'ah. Some Takaful operators offer crop Takaful and also livestock Takaful. But, majority of the clients do not include poor and those living in rural areas.

Microinsurance is being offered in microfinance institutions. Separate statistics for Islamic insurance are not provided by Pakistan Microfinance Network. But, it estimates that the share of Islamic micro-financial services is between 10% to 15% in various segments. Table 4 shows the outreach statistics of microinsurance in Pakistan.

**Table 4: Outreach Statistics of Microinsurance**

Province/Region	Microinsurance	
	Policyholders	Sum Insured (Rs.)
AJK	110,401	6,090,558,060
Balochistan	46,260	4,604,589,788
Gilgit-Baltistan	54,977	8,701,369,541
FATA	24,908	1,046,105,935
Islamabad	121,695	6,771,399,733

KP	253,304	15,184,984,085
Punjab	6,207,563	271,550,997,503
Sindh	2,068,903	70,182,898,006
Total	8,888,011	384,132,902,651

**Source: Pakistan Microfinance Network**

In the last few years, the government has launched a public health insurance system whereby an individual who is citizen of Pakistan can avail health services and assistance from the panel hospitals free of any charge. The program is known as Sehat Sahulat Program.

Any citizen of Pakistan can send his/her national identity card number in SMS to 8500 and check for eligibility in the program. So far, a total of 37,294,021 families have enrolled in the program. As many as 5,017,972 total hospital visits had been reported by November 2022. There is a very vigilant and active complaint management system. So far, 89,617 complaints have been received. Out of that, 88,621 had been resolved with a satisfaction rate of 97%.

Coverage for secondary care is capped at Rs. 60,000 per family per year. Additional coverage of Rs. 60,000 per family is also included. Secondary care includes in-patient services, emergency treatment requiring admission, maternity services, fractures and injuries. Local transportation cost of Rs. 1,000 (thrice per year) is also included.

Coverage for priority care is capped at Rs. 300,000 per family per year. Additional coverage of Rs. 300,000 per family is also included. Priority care further includes heart diseases (angioplasty or bypass), diabetes, burns, limb saving treatment, implants, prosthesis, end stage kidney diseases or dialysis, chronic infections (hepatitis/HIV/rheumatology), organ failure (liver, kidney, heart, lungs), cancer (chemo, radio, surgery) and neurosurgical procedures.

It is a cashless system with real-time monitoring. Panel hospitals include a mix of private and public hospitals to ensure access and allow competition to improve service delivery.

To avoid moral hazard, standard rates for different kinds of treatments are devised. Hospitalization is offered in general ward to efficiently utilize the resources.

With time, the system may introduce filtering and take small premiums from the people who can afford. However, right now, the universal health coverage has no filtering and everyone is covered for health expenses.

NADRA database is used for verification. People with disabilities and transgender are also included. To monitor the quality of service, there is a comprehensive feedback mechanism developed with physical and online resource deployment. There is one counter in every panel hospital for information, documentation and monitoring. Customers are asked to evaluate the services used.

There is mandatory audit post discharge. Any complaints will be escalated step by step to higher-ups if unattended and unresolved. Panel hospitals will be evaluated on a 1,200 set of indicators. There is threat of losing panel membership if complaints are frequent and remain unattended and unresolved.

### 3.2.3. Outreach of Waqf

Waqf is managed by the Auqaf and Religious Affairs Department in the provinces. The main job of Auqaf Department is to safeguard the endowed properties. The properties are in the form of:

- ❖ Masajid
- ❖ Shrines
- ❖ Residential plots
- ❖ Shopping plazas
- ❖ Agricultural lands

Some of the properties are leased to the bidders for a finite duration. Ownership remains with the Chief Waqf Administrator. KP Auqaf Department has also started e-Bidding process. Some of the prominent completed projects include the following:

- ❖ Auqaf Plaza Dabgari Garden, Peshawar
- ❖ Auqaf Toraqul Plaza Shaheen Bazar, Peshawar
- ❖ Darul Auqaf Peshawar, Saddar
- ❖ Auqaf Office Complex, Eidgah Charsadda Road, Peshawar
- ❖ Auqaf Auditorium, Eidgah Charsadda Road, Peshawar
- ❖ Auqaf Bukhari Baba Complex Shami Road, Peshawar
- ❖ Auqaf Shopping Center, Charsadda
- ❖ Auqaf Shopping Plaza, Charsadda
- ❖ Auqaf Plaza Bannu Road, Dera Ismail Khan

Some of the projects in the pipeline are listed in Table 5 along with details of the projects, size of the projects and estimated costs.

**Table 5: Details of Auqaf Developmental Projects in Pipeline**

No.	Name of Site	Cost (mln Rs.)	Description of Building
1	Waqf plot adjacent to Masjid Mohabat Khan, Peshawar	2.43	A 4-storey building having 5 shops at each storey shall be constructed
2	Waqf property Katra adjacent to Masjid Mohabat Khan, Peshawar	111.56	A 7-storey building having 176 shops shall be constructed
3	Waqf Bukhari Baba Complex, Shoba Bazar, Peshawar	245.00	A 5-storey building having 35 shops and 10 flats shall be constructed

4	Waqf property Namak Mandi, Peshawar	4.54	A 4-storey building having 2 halls at each floor shall be constructed
5	Waqf property Bazar Kalan, Peshawar	5.60	A 5-storey building having 3 shops at each floor shall be constructed
6	Waqf property Yousaf Abad, Dalazak Road, Peshawar	52.00	A 5-storey building having 36 shops and 20 flats shall be constructed
7	Waqf property Shah Wali Qatal Qissa Khwani Bazar, Peshawar	22.00	A 4-storey building having 12 shops and 8 flats shall be constructed
8	Waqf property located at Circular Road, Yakatoot Peshawar	85.00	A 5-storey building having parking in basement, 12 shops at ground floor and wedding/gathering hall at subsequent floors shall be constructed
9	Waqf property Ganj Ali Khan, Peshawar	32.00	A 5-storey building having 6 shops in basement, ground and first floor shall be erected and 2 flats shall be constructed at first and second floor
10	Waqf plot Dodhyal, Mansehra	41.00	A 4-storey hostel building having 15 rooms with allied facilities of kitchen, washrooms, laundry, etc shall be constructed
11	Waqf plot Bagheecha, Abbottabad	125.00	4 villas of 3 storey each having 2 flats each shall be constructed at different contour levels.
12	Waqf plot Gul Baba Tangi, Charsadda	62.00	64 shops will be constructed
13	Waqf plot adjacent to Masjid Adil near Kacheri Bank Road, Mardan	32.00	12 residential flats shall be constructed at different floors

### Appendix 3.1: Estimation of Potential Zakat Collection in Pakistan

This section provides a primer on estimation of potential Zakat collectible in Pakistan using actual and recent data as much as possible.

#### *Zakat Computation on Gold*

It is difficult to obtain micro data on gold holdings in Pakistan from aggregate indicators. For this reason, proxy data has to be used. There are a total of 31,915,884 housing units in Pakistan as per 2017 Census. Total owned units with minimum of three rooms are 10,596,504 as per 2017 Census.

It is estimated that a household living in owned housing unit with minimum of three rooms will on average possess 200 grams of gold. Some households will own more or less than this, but for Pakistan, this assumption seems to be close to the mean value based on pilot survey results in Karachi.

With these estimates, Rs. 30.138 trillion is the Zakatable value of gold in Pakistan taking the current price of gold into consideration (Rs. 14,228 per gram on Forex.pk accessed on January 23, 2023).

The estimates shared with Economic Coordination Committee (ECC) point towards potential private gold holdings of 5,000 tons (Source: Business Standard & Express Tribune, February 20, 2022). Therefore, our estimate of 2,119.38 tons is not overly optimistic.

The estimates shared with Economic Coordination Committee point towards potential private gold holdings of 5,000 tons.

There is another alternate way to estimate private gold holdings. There are roughly 41,358,490 married females in Pakistan excluding widowed and divorced as per the reported statistics in Census 2017.

If upper middle income class poverty line is used at Purchasing Power Parity (\$5.50/day), then 75.4% of them can be excluded as relatively poor. For the remaining 24.6%, if average gold holding of 200 grams per married female is used, then Rs. 28.95 trillion worth of gold is estimated to be held by married females.

In addition to that, there will be unmarried females who would also have gold holdings. Therefore, private gold holdings from these two proxies can be estimated to range between Rs. 29 trillion to Rs. 30 trillion. We can take the average of these two estimates to come up with a potential figure of Zakat collectible on gold holdings.

#### *Zakat on Real Estate Value and Rent*

The World Bank estimates that around 60% to 70% of Pakistan's wealth is in real estate. Pakistan's nominal GDP is roughly \$376 billion in reported accounts. There are various estimates about the size of the informal and unreported economy.

Taking a conservative approach and relatively more consensus-based figure, it is estimated that one-third value of GDP is in the informal and undocumented sector. World Inequality Database estimates that Pakistan's wealth-income ratio is 5.5. It can give us an estimated value of real estate wealth, i.e. approximately \$1.32 trillion.

World Inequality Database estimates that top 1% wealth owners hold 25.8% of wealth in Pakistan. If only 10% of real estate wealth is considered as held for trade in excess of regular personal use, then the held for trade real estate wealth can be conservatively estimated at Rs. 31.02 trillion at PKR/\$ exchange rate of Rs 235. If 2.5% rate of Zakat is applied on it, the potential Zakat collectible on real estate wealth can be estimated.

It is estimated that average rental yield in Pakistan is 4% as per average rate obtained from Graana, Zameen and other real estate platforms. Census of 2017 provides the data that 11.53% of all housing units are rented in Pakistan.



Applying this 11.53% to total estimated real estate value, we can obtain the estimated base of real estate wealth that is rented. Applying 4% average annual rental yield, we can obtain the Zakatable base of aggregated rental income in Pakistan. We can apply 2.5% rate of Zakat to obtain potential Zakat collectible on rental income.

#### *Zakat Computation on Tradable Inventory*

It is very hard to compute the value of unsold inventory at a particular date. Wholesale and retail trade value in GDP is reported for each financial year. Assuming one-month inventory outstanding from the total annual value of production, we can estimate the Zakat base. Thus, we are assuming average inventory turnover ratio of 12. We can apply 2.5% rate of Zakat on the estimated value of tradable inventory to come up with a potential figure of Zakat collectible on tradable inventory.

#### *Zakat Computation on Value of Financial Investments*

People also hold their wealth in bank accounts, mutual funds, stocks, annuities, and national saving scheme instruments. World Inequality Database estimates that top 20% wealth owners own around 74.2% of wealth in Pakistan.

Among the individual heads related to financial investments, if only the wealth held by the top 20% is assumed to be subject to Zakat where the payer has Nisab level value of wealth in excess of personal needs and debts, the total Zakatable base on each of the financial investment heads can be estimated.

A 2.5% rate of Zakat can be applied on the estimated aggregated value of financial investments held by top 20% wealth owners to come up with a potential figure of Zakat collectible on financial investments. The source and date of data obtained in various categories is mentioned in the estimation table.

Most of the investments in shares in Pakistan are made by institutional investors who regularly trade shares in the market. Therefore, the market capitalization of PSX can be taken and adjusted with respect to wealth distribution data from World Inequality Database as described previously. A 2.5% rate of Zakat can be applied on total market capitalization to obtain a conservative estimate of potential Zakat collectible on shares.

#### *Zakat on Livestock Value*

Livestock population data is available in Economic Survey of Pakistan 2020-21. Applying average market value on these livestock categories, the aggregate value of livestock can be estimated. World Inequality Database estimates that top 20% wealth owners own around 74.2% of wealth in Pakistan.

If only the wealth held by the top 20% is assumed to be subject to Zakat where the payer has Nisab level value of wealth in excess of needs and debts, the total Zakatable base on livestock can also be estimated. The rates on livestock wealth differ depending on whether the animal is goat, cow or camel. However, as argued by Yusuf al-Qardawi, the average rate can safely be

taken as 2.5% for a preliminary potential Zakat estimation exercise since it is not assessment of Zakat for a particular individual.

#### *Ushr on Production*

Economic Survey of Pakistan 2020-21 reports that 19.90 million hectares of cropped area out of 24.1 million hectares is irrigated by canals, wells, canal wells, tube wells and canal tube wells. Hence, it can be inferred that 82.57% of the cropped area in Pakistan obtains water supply from irrigation.

On the other hand, 17.43% of the cropped area in Pakistan obtains water supply from natural sources such as rain. Assuming constant returns to scale on average, the Nisf Ushr and Ushr can be applied on the value of agricultural produce to estimate the potential of Ushr collectible in Pakistan.

In the classical understanding, only the production from land is subject to Ushr. Fish catch and poultry production is subject to Zakat if held for trade. Assuming inventory turnover ratio of 12, only one-month production value is assumed to be subject to Zakat from the total annual value of production. If 2.5% rate is applied on tradable inventory, the potential collection can be estimated on fish catch and poultry and dairy production.

**Table 6: Estimation of Zakat**

Report Date	Category	Notes and Sources	Amount (Mln Rs.)	Zakat (Mln Rs.)
	Zakat on Wealth			
	Gold	Interpolation from Census 2017	30,138,153	559,063
End Dec 2022	Currency in Circulation (Stock)	SBP Data	7,829,645	145,240
End Dec 2022	Deposits in Personal Category	CA (33%), SA & TD (67%). Wealth Held by Top 20%	18,878,266	350,192
End Dec 2022	Non-Resident Deposits in Personal Category	CA (33%), SA & TD (67%). Wealth Held by Top 20%	1,211,940	22,481
End Dec 2022	KSE Market Capitalization	Net Zakatable Base. Source: PSX	6,500,828	120,590
End Dec 2022	Real Estate Value (1.32\$ Trillion With Wealth-Income Ratio of 5.5)	10% of Real Estate Wealth Considered Held for Trade	31,020,000	775,500
End Dec 2022	Rental Income (Assumed Yield=4%, 11.53% Houses Rented)	11.53% Rented Units With 4% Yield	2,241,340	56,034
End Dec 2022	Open End Funds	MUFAP	1,530,691	28,394
End Dec 2022	Dedicated Equity Funds	MUFAP	0	0
End Dec 2022	Voluntary Pension Schemes	MUFAP	43,219	802
End Dec 2022	Exchange Traded Funds	MUFAP	684	13
End Jun 2020	Outstanding Value in NSS	SBP Handbook	3,608,000	66,928
End Dec 2022	Foreign Exchange Deposits (FE-25)	SBP Data	1,520,450	28,204
End Sep 2022	Insurance Premium/Contribution (Non-Life)	Insurance Association of Pakistan	113,665	2,108

ISLAMIC SOCIAL FINANCE FOR SOCIAL PROTECTION IN PAKISTAN

End Sep 2022	Insurance Premium/Contribution (Life)	Insurance Association of Pakistan	227,095	4,213
End Sep 2022	Insurance Premium/ Contribution (Family Takaful Business)	Insurance Association of Pakistan	26,302	488
End Jun 2021	Trade Assets (1-month value of Wholesale + Retail Trade + Exports)	1-Month Inventory	1,038,417	19,263
End Jun 2021	Livestock Value (Cattle at Rs. 100,000/Unit)	51,500,000	5,150,000	95,533
End Jun 2021	Livestock Value (Buffalo at Rs. 100,000/Unit)	42,400,000	4,240,000	78,652
End Jun 2021	Livestock Value (Sheep at Rs. 20,000/Unit)	31,600,000	632,000	11,724
End Jun 2021	Livestock Value (Goat at Rs. 20,000/Unit)	80,300,000	1,606,000	29,791
End Jun 2021	Livestock Value (Camel at Rs. 100,000/Unit)	1,100,000	110,000	2,041
	<b>Total Wealth Zakat</b>			2,397,253
	Zakat and Ushr on Produce			
End-Jun 2021	Production in Livestock Sector (Dairy, Meat, Poultry, etc.)	1-Month Inventory	5,509,11	11,477
End-Jun 2021	Fish Catch	1-Month Inventory	185,701	387
End-Jun 2021	Produce on Rain-fed Land (17.43% Cropped Area)	Ushr on Value of Production	809,233	80,923
End-Jun 2021	Produce on Irrigated Land (82.57% Cropped Area)	Nisf Ushr on Value of Production	3,833,529	191,676
End-Jun 2021	Production in Forestry	Nisf Ushr on Value of Production	244,184	12,209
End June 2021	Mining and Quarrying	Nisf Ushr on Value of Production	976,819	48,841
	<b>Total Zakat and Ushr on Produce</b>			345,514
	Total Zakat Collection	2,742,767		
	Total GDP at Market Prices (2020-21)	66,949,907		
	Zakat to GDP Ratio	4.10%		

## Chapter 4

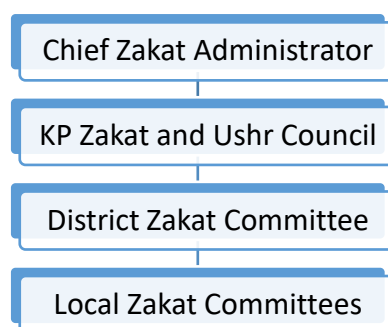
# Governance and Challenges in Islamic Social Finance in KP

### 4.1. Zakat Administration Structure

First, a brief introduction of the hierarchical structure of Zakat administration in KP province is provided. In the governance structure, Chief Zakat Administrator is at the top. Then, there is Additional Secretary Zakat and Ushr Department. Then, there is Deputy Administrator Admin and Deputy Administrator Audit.

KP Provincial Zakat and Ushr Council is the apex authority. Then, there are district Zakat committees and at the bottom of the hierarchy are local Zakat committees which perform bulk of the work in screening, determining eligibility and ensuring timely disbursements.

**Figure 8: Zakat Administration Structure**



There are around 50,000 volunteers involved in Zakat distribution process currently in 4,400 local Zakat committees. In the lower tier of Zakat administration at the district level, there is audit staff and field clerks, also known as group secretaries.

The Zakat and Ushr Department does not collect Zakat directly. It is allocated a share from central collection. KP province gets approximately 15.8% share in total Zakat collection. As of now, it only screens and manages disbursement of Zakat funds which are received from the central Zakat collection at the federal level.

There are around 50,000 volunteers involved in Zakat distribution process right now in 4,400 local Zakat committees.

After the 18th Amendment, the collection of Zakat and Ushr is to be carried out by the provinces. As of now, collection at the provincial level is not significant at all.

#### 4.1.1. Structure and Operations of District Zakat Office

In each district, a District Zakat and Ushr Committee is constituted by Zakat and Ushr Council. The District Committee consists of a Chairman, District Social Welfare Officer and two women from the district, who shall not be less than forty-five years of age, and one non-official member from each tehsil or sub-division in the district.

The District Zakat Officer shall also be the Secretary of the Committee. The Chairman shall be nominated by Zakat and Ushr Council and members shall be nominated by Zakat and Ushr Council in consultation with Chairman. The District Committee shall hold meetings at least once every three months.

The District Zakat Chairman is appointed by KP Zakat and Ushr Council and works voluntarily. Appointment is for three years, extendable to another three-year term only. Members of district Zakat committee shall be nominated by Zakat and Ushr Council in consultation with the Chairman. The Chairman has a car at his disposal and gets fuel allowance of Rs. 3,000 every six months. In one-to-one key informant interviews, it was found that a section of the population has a perception that the Chairman is politically appointed.

Working under the Chairman at the district level, there is senior district Zakat officer and district Zakat officer. They are assisted by an assistant (employed in Grade-16), stenographer (employed in Grade-14), senior clerk (employed in Grade-14) and junior clerk (employed in Grade-11).

As per clause 10 of Section 14 of the Zakat and Ushr Act, 2011, it is mandatory for the district Zakat committee to hold meetings at least once every three months. In focus group discussions, multiple districts shared that it is a norm that one meeting is held at a minimum every two months in district Zakat office.

Zakat paid staff is paid fixed salaries from 10% of total Zakat funds. Zakat paid staff includes:

##### **Auditors**

- ❖ Audit Officer (Salary Rs. 25,000 per month)
- ❖ Auditor (Salary Rs. 20,000 per month)
- ❖ Audit Assistant (Salary Rs. 19,000 per month)

**Group Secretary/Field Clerk** (Salary Rs. 17,000 per month)

#### 4.1.2. Role of Group Secretary

The group secretary or field clerk comes under paid staff. Their salaries are paid from Zakat funds and fixed at Rs. 17,000 per month. The staff, during interviews, shared that there has been no increment in the salary for the last several years. Their employment is also contractual. They are not given government grades and permanent employment.

When inquired about the same concern, the district Zakat management shared that to compensate for low salary, group secretaries are not required to come to office every day. They are required to come once in a week. They also do not have designated chair and computer for work in the district Zakat office.

The main job of group secretary includes these important functions:

- ❖ Maintain and strengthen liaison between district Zakat committee and local Zakat committee.
- ❖ Be part of election process.
- ❖ Clarify law when needed by local Zakat committees.
- ❖ Feed data on Zakat Information Management System.
- ❖ Keep record of registers, such as LZ-11, LZ-12, LZ-13 and LZ-19 at the time of audit.
- ❖ Hand over LZ-11 to LZC chairman.

One issue in the work design of group secretaries is idle labor hours since major activity is in Guzara allowance and disbursement takes place twice a year.

#### 4.1.3. Local Zakat Committees: Formation and Functions

##### 4.1.3.1. Formation of Local Zakat Committees

Local Zakat committee has nine members including seven males and two females as defined in clause 3 of Section 15 of Zakat and Ushr Act, 2011. The female members must be at least 45 years old. Local Zakat committee chairman and vice chairman need to be members of local Zakat committee. All members shall have matriculation degree, but in case, this condition cannot be followed, at least the chairman has to be matriculate.

All members work voluntarily. However, local Zakat committee chairman is allowed Rs. 1,500 allowance for printing, photocopy and stationary. In a locality with 10,000 or more people, there must be one local Zakat committee covering that area. One local Zakat committee shall be formed for five villages. There are different criteria for rural and urban locations so as to cater to the dynamics of rural and urban demographics. A local Zakat committee after formation continues to operate as long as it has five members.

##### 4.1.3.2. Local Zakat Committees Election

Selection, election and administrator are options to form local Zakat committees, as revealed through focus group discussion with the key informants. Normally, local Zakat committee chairman is elected for three years through an election conducted by district Zakat committee in a mosque or government school.

Election date and venue is communicated in advance by the presiding officer. Mode of communication includes using notices in mosques. In some places like Abbottabad, it was

discovered that ticker on cable TV channel and newspaper notice was also used as a medium to popularize the election process.

Election is supervised by four key individuals: Imam of mosque, district Zakat officer, gazetted government officer and group secretary. Local Zakat committee member winning most votes becomes chairman and the second one becomes vice chairman. In case local Zakat committee chairman resigns, then the remaining members elect new chairman from among themselves.

Clause 4 of Section 15 of Zakat and Ushr Act, 2011 requires that the team constituted by the district committee shall organize a separate gathering of the adult Muslim female residents of the locality and call upon them to select, in the prescribed manner, two Muslim women residing in that locality who are known to be pious and who enjoy their trust to be members of the local committee.

#### 4.1.3.3. Local Zakat Committees Mandate and Work

Primary task of local Zakat committee is to identify deserving beneficiaries and ascertain Istehqaq (eligibility for assistance). Every Mustahiq (deserving) applicant applies to local Zakat committee.

Local Zakat committee usually meets one or two times in a mosque or residence of chairman, vice chairman or any member. Efforts are also made to engage female members to help in identifying female Mustahiq. The age requirement for females helps in engaging those women in local Zakat committees who can be active, social and well-known.

Since many Mustahiq are not literate, local Zakat committee chairman and members fill the Istehqaq form after due verification of details.

Local Zakat committee chairman and vice chairman are authorized signatories on the cheques given to the beneficiaries. They hand over the cheques to the beneficiaries and some even go to the bank to facilitate them.

They also maintain records in registers, such as:

- ❖ LZ-11 (List of approved beneficiaries with CNIC copy and sign)
- ❖ LZ-12 (Payments list beneficiary-wise)
- ❖ LZ-13 (Main cashbook)
- ❖ LZ-19 (List of all Zakat applicants whose forms were submitted)

#### 4.1.3.4. Issues in Local Zakat Committees

Even though the rules of formation aim at diversification, but not all members participate actively, especially females, in culturally traditional areas or regions.

Since there is no remuneration involved, many people do not show keenness to become members of local Zakat committees. It was learnt during the key informant interviews that some who do participate in local Zakat committee affairs, may do so because they have other motives as well, such as creating a good social image which can help in political pursuits.

Another important issue for female members is the requirement of matriculation. Law makes it necessary that every member shall have matriculation degree. Even though female education and enrolment numbers have improved in the province; however, in many regions, there are very few old women who have completed matriculation. Thus, not all members have matriculation degrees, especially elderly females.

In some areas, it was relayed by the respondents in key informant interviews that local Zakat committee chairman and vice chairman are selected on political grounds. When members of LZCs as well as DZCs are appointed/selected by the ruling party setting aside the criteria or rule of selection, it actually compromises the transparency and integrity of the whole Zakat disbursement system. Naturally these politically appointed members then resort to political favoritism in selection of the beneficiaries.

Many people are of the view that the ruling government uses Zakat administration to keep their political workers busy.

Another very important issue is the increase in coverage of local Zakat committees due to huge increase in population in urban districts. Population in some regions has increased exponentially. This may require forming more local Zakat committees in order to ensure broad coverage in screening and identification process and also in auditing later on.

The increase in urban population requires forming more local Zakat committees in order to ensure broad coverage in screening and identification process and also in auditing later on.

It was also learnt in some districts that some committees were inactive in districts where governance and law and order is weak. Some local Zakat committees do not have chairman due to local body elections.

Some local Zakat committees have formed unions in some districts and they protest due to their grievances. As a result of protests and halt in work, beneficiaries suffer as funds are neither disbursed nor returned by local Zakat committees. This is because signatures of chairman and vice chairman are required on cheques. To overcome such issues, an administrator is tasked with carrying out disbursements if local Zakat committees are not able to work and have unresolved conflicts in some areas.

#### 4.1.4. Zakat Programs and Outreach

##### 4.1.4.1. Funds Allocation in Different Programs

1. Guzara allowance (Rs. 12,000 per beneficiary for a year).



2. Marriage assistance grant (Rs. 30,000 one-time payment; age limit 35).
3. Educational stipend
  - a. Schools, colleges and universities.
  - b. Deeni Madaris (Rs. 3,000 per month for resident and Rs. 2,000 per month for non-resident students).
4. Health
5. Healthcare grant (Rs. 10,000 for indoor and Rs. 5,000 for outdoor patients).
6. Special healthcare grants (Rs. 50,000 to Rs. 300,000 or more) for those Mustaheqeen-e-Zakat patients who suffer from four chronic diseases, i.e. cardiac, cancer, neuro and kidney diseases, for which funds are not available/insufficient in provincial level hospitals/institutions.
7. Vocational and technical training (discontinued since 2018).

#### 4.1.5. Issues in Mustahiq App and Website

One great initiative by the KP Zakat and Ushr Department is the launch of the Mustahiq app. Tapping the youth bulge and increased penetration rates of internet connectivity, smartphone usage and multi-lingual interfaces in app design, the KP Zakat and Ushr Department launched the Mustahiq app with information in Urdu, Pushto and English.

Currently, the app user can access information on local Zakat committees in different areas, direct phone number of local Zakat committee chairmen and also see the different programs and schemes which are funded from the Zakat funds in KP.

As of now, it is not possible to submit application through the Mustahiq app or website. Another shortcoming, on the website in particular, is that all the information is in English.

Forms in the Mustahiq app are in English as well except for Guzara allowance. Currently, the app or website is not used for notice of enrolment and disbursement to the beneficiaries.

Lastly, the app does not help the Muzakki in any way in terms of Zakat information, calculation, assessment and payment. There is no Zakat calculator. There is also no mechanism of payment of Zakat through the app. There is no mention of bank account in which Zakat can be paid voluntarily. Also, there are no notices or push notifications to encourage payment of Zakat.

#### 4.1.6. Problems in Zakat Administration

##### 4.1.6.1. From Muzakki Perspective

From the perspective of Muzakki (Zakat payer), there are following important problems in Zakat administration:

*Lack of Awareness about Zakat Rules*

People who are required to pay Zakat often do not have any information on how much Zakat to pay on different categories of assets. They are also not aware of the personal assets which would be considered exempted and those which would not be considered exempted from Zakat. Complications arise regarding status of Zakat in joint properties, real estate, and financial assets.

There is no assistance available for Zakat assessment at head office and district office since collection is not decentralized at all at the moment. The staff does not receive any training on Zakat rules and assessment. If the collection function is also integrated in the role of department, staff training would be vital in future to help people in Zakat assessment.

Formal annual reports are not published. Only summary statistics are available on website for the most recent year only. No visual documentation of events, newsletters or corporate video of the department were found on the website.

Most people are also not aware that the government has a dedicated bank account into which Zakat can be paid and it has identified beneficiaries at the grassroots level. So far, there is no connecting mechanism between Muzakki and Mustahiq.

*Minimal Coverage of Zakatable Assets*

Most assets and wealth forms in First Schedule of KP Zakat and Ushr Act, 2011 represent financial assets and wealth forms which are in the documented sector and where it is possible to deduct Zakat at source. Excluding other assets and wealth forms for involuntary collection results in inadequate collection in comparison to the funds required to be paid to the targeted beneficiaries.

*Trust Deficit*

There is a huge deficit of trust between Muzakki and Zakat collecting agency. In a centralized government-run system, Muzakki generally feels that either the Zakat funds would not be spent transparently and even when they are used in social assistance, formal juristic requirements may not be met. Hence, trust deficit is still there with respect to:

- i) Transparent utilization of funds.
- ii) Shari'ah-compliant distribution which ensures Tamleek (asset ownership).
- iii) Payment to the deserving beneficiary who is Mustahiq from Shari'ah perspective.

*Inexact Incidence*

What causes further distrust is inexactness in incidence. Complexity in adjustments/refunds if people wish to claim adjustment or refund in lieu of private Zakat payment or in case Zakat was deducted at source by deducting agency, such as banks, while people were not Sahib-e-Nisab.

Zakat is now mainly deducted from remunerative bank accounts and financial wealth and profits on financial investments. Zakat is deducted at source by collecting agency, such as bank, mutual fund, corporation, etc. But, these collecting agencies do not have the complete picture of net wealth of the person from whose wealth and profit they are deducting Zakat.

Hence, it is very much possible that more or less Zakat is deducted than necessary as the law does not allow collecting agency to deduct Zakat on other broader forms of wealth, such as foreign currency accounts, current accounts, gold, silver, etc.

#### *Complexity in Adjustments/Refund*

Even though there is provision for refund, but due to complex process and red tape, people tend to avoid having to pay Zakat to the government by either keeping very low cash on pre-announced Zakat deduction date or by submitting a simple affidavit that they shall be exempted from Zakat deduction.

Initially, this right to submit affidavit and claim exemption was allowed to particular schools of thoughts which had a different juristic understanding of the rules and scope of Zakat altogether. But, eventually, upon public resistance, it was allowed to all as per clause 3(a) of Section 1 of KP Zakat and Ushr Act, 2011.

#### *Dual Burden*

Since there is no tax incentive for Zakat payer to get relaxation in taxes, people underreport their income and wealth to avoid dual burden of taxes and Zakat. However, since Zakat is obligatory from a religious perspective, people feel comfortable in distributing Zakat funds to the people in their close social circle or the institutions in which they have more trust or with which they have communal/religious affinity.

#### 4.1.6.2. From Mustahiq Perspective

From the perspective of Mustahiq (Zakat receiver), there are following important problems in Zakat administration:

##### *Lack of Impactful Donation – Inadequacy of Benefit Size*

Majority of the funds allocated to the province are disbursed through cash assistance under Guzara allowance. As of now, the monthly assistance turns out to be Rs. 1,000 per family. The amount is just 4% of the minimum monthly wage for the unskilled workers in the province. Such a meagre amount of assistance hinders socio-economic mobility. There is a need for some sort of benchmarking mechanism for the benefit size. Neediness is checked in Istehqaq form, but the person is either given full assistance of Rs. 1,000 per

Due to ineffective coverage, the monthly assistance under Guzara allowance is just Rs. 1000 per month, which is just 4% of the minimum monthly wage for the unskilled workers in the province. This meagre amount, too, is given to disabled, widows, orphans and old-age people on priority basis.

family per month or not given anything at all. Not all the eligible people would still be having same level of neediness, but the disbursement is uniform among all Mustahiq regardless of their intensity of neediness.

#### *Ineffective Coverage*

Access to assistance is also hindered by ineffective coverage. Due to lack of funds, priority is given to disabled, widows, orphans and old-age people first as suggested in clause (a) of Section 8 of Zakat and Ushr Act, 2011. Of course, people in poverty not having these particular unfortunate circumstances are also great many in number. But, due to lack of funds, they are unable to get assistance.

#### *Small Assistance Leads to Consumption*

One-time small cash assistance leads to complementing consumption at best. Beneficiaries cannot make productive investments in their education and skills. Thus, they remain trapped in having dearth of required skills and capital for any meaningful employment or self-employment prospects.

Guzara allowance is unconditional transfer. Unconditional cash transfers are less impactful to achieve socio-economic mobility as compared to conditional transfers. In the past, in some local Zakat committees, the previous list was not updated and there was no current neediness check performed on the beneficiaries every year. This means that the person who was part of the beneficiaries list last time, he/she was kept in the list without checking the current neediness status.

The situation has greatly improved now through reforms introduced by the Zakat Department. Some of these reforms include verification at head office level. Also, the duplications are avoided by checking a person's records in BISP and NADRA. An objective and quantitative neediness criteria is implemented to decide about eligible beneficiaries through objective scoring.

Zakat funds are received once a year by the department. From the time of collection to disbursement, there is a time lag. Also, the funds are not available year round to meet the social protection needs of the beneficiaries at different times of the year.

#### *Halt in Technical Education*

Since 2018, provision of technical education through Zakat funds has been stopped. Such education can enhance skills to enable gainful employment to the passing trainees.

#### **4.1.6.3. From Government Perspective**

From the perspective of collecting intermediary or regulator, there are following important problems in Zakat administration:

*Declining Central Collection*

Adjusting for value of currency, population and economy, the collection of Zakat in the federal pool is declining. Hence, this affects allocation to the provinces as well. There is decline in disbursement of funds to the provinces and districts. That is why, the institution of Zakat has become weak for socio-economic mobility and poverty reduction.

For comparison, the KP government had a Zakat allocation of roughly Rs. 1 billion in the outgoing year. On the other hand, BISP has a size of Rs. 260 billion.

*Complexity in Assessment*

Zakat is a charge taken from people's wealth and unused earnings. There are many juristic differences and complexities which make the assessment of Zakat difficult to handle at the central level. Keeping in mind cost of collecting information and assessment, the government has taken the safe route to confine Zakat deduction from declared financial wealth and earnings in the First Schedule of the KP Zakat and Ushr Act, 2011.

Even though the Second Schedule mentions many other asset classes and wealth forms on which Zakat is due, but the government avoids cost and complexity of assessing Zakat on those forms of wealth and asset classes.

*Inadequate Administration*

If coverage of Zakat is broadened by the government to collect greater part of obligatory Zakat itself, it needs to have machinery and documentation to make this happen.

As of now, the economy is largely undocumented. The government's administrative capacity is also weak. Even the revenue department has not been able to increase the tax-to-GDP ratio significantly over the course of the entire history since independence.

It can be argued that Zakat is a religious obligation and hence people will not try to evade it. It is true to a large extent; however, it does not mean that they will agree to pay Zakat to the government. They pay Zakat in their private capacity ensuring that Zakat funds go directly to the beneficiary without official and unofficial administrative bottlenecks in a government-run system.

Unlike the resources which the FBR has, the Zakat Department does not have enough human resources, infrastructure and departmental funds to play a direct role in assessment and collection. Since only the asset and wealth forms in the First Schedule are subject to involuntary Zakat collection, the provincial Zakat departments do not have a role to assess and collect Zakat in other wealth forms which are mentioned in the Second Schedule.

The segregation of asset and wealth forms in the First and Second Schedule is made due to this administrative hurdle. Only the selected financial assets in the First Schedule are subject to

involuntary Zakat deduction at source where there is not much need for active assessment and collection.

#### *Exemption Granted to Everyone Unconditionally*

The fundamental reason why Zakat collection at central level declined is because now unconditional exemption is allowed from Zakat payment to anyone who submits an affidavit.

Private banks, investment companies, brokerage houses and insurance agents, in a competitive struggle to win customers, facilitate their clients in submitting this affidavit. People opt for getting exemption in order to avoid perceived misuse of Zakat funds or cut in Zakat spending due to high cost of administration of government-run Zakat system.

What has further fueled this sentiment is that both religious and secular NGOs thrive on philanthropic giving rather than support of government which faces deficit year after year. Thus, religious scholars have, by and large, given way to the viewpoint that it is not necessary to pay Zakat to the government even if the government has a formal system of Zakat collection.

#### *High Overall Cost of Administration*

One reason of distrust between Muzakki (Zakat payer) and government as collecting intermediary is that people perceive the government institutions to be over-staffed and inefficient from the perspective of cost efficiency.

It was found during this research that overall cost of Zakat administration including cost of running the head office operations and paying employees who are employed on non-Zakat funds at various levels is roughly Rs. 350 to Rs. 400 million per year. Adding 10% Zakat funds from which paid staff is paid salaries, the overall cost of administration turns out to be almost 50% of total Zakat allocation to the KP province in the outgoing year, i.e. Rs. 500 million expense for roughly Rs. 1 billion Zakat allocation in economic terms.

It must be kept in mind that all these expenses are not covered from Zakat alone. Only the salaries of group secretaries and auditors are paid from the Zakat funds. Rest of the expenses are covered from the government grants and budget allocation. As per sub-clause (i) of c in Section 8 of Zakat and Ushr Act, 2011, expenditure on the administrative organization of the Chief Administrator, the Zakat and Ushr Council, and a District Committee shall be met by the government.

However, from the economics point of view, the overall collection and disbursement is roughly 50% of the total economic costs involved in Zakat administration, no matter how that cost is funded. Hence, there is a need to increase the collection.

#### *Delay in Receipt of Zakat Funds to Provinces and Districts*

In the last few years, the release of Zakat funds from the federal government to the provinces has been delayed. This also results in delay of transfer to districts and then eventually to

beneficiaries. Even though Zakat on financial assets is deducted on 1st Ramadan, but the payment to provinces is delayed for several months.

#### 4.1.7. Identification and Selection of Beneficiaries

It is the primary job of local Zakat committee to determine Istehqaq (eligibility for assistance). Currently, due to limited funds, only the disabled, widows, orphans and senior citizens are prioritized in Guzara allowance. It is easier to ascertain these eligibility characteristics.

In order to be eligible, disabled people should have disability certificates and special mention of disability in Computerized National Identity Card (CNIC). Widows should furnish death certificate of their deceased husbands to become eligible. Orphans also need to submit death certificate of their father. Lastly, age of senior citizens is verified from CNIC. On the other hand, marriage assistance applicant needs to submit Nikah Nama (marriage certificate) if marriage is solemnized recently.

Those who are already beneficiaries of the Benazir Income Support Program (BISP) are currently avoided in the selection of beneficiaries to prevent duplication. It was learned during the briefing sessions with the top management of the Zakat administration that there is a plan to relax the condition in the near future. The Zakat and Ushr Department has developed a database of 550,000 people who have applied for Zakat assistance. It is a great example of making outreach more effective and efficient. This can also help in avoiding adverse selection as well as in impact assessment with useful data about the beneficiaries in the database.

For Guzara allowance, the head office performs a second screening on a point-scoring system, giving more points to inopportune circumstances. For instance, if a person is senior citizen and disabled with dependent family members and no work, he will be given more points. A person with more dependent family members and unfurnished residence with no or limited utilities supply will get more points.

In educational stipends, the scholarship committee comprises head of institution, class teacher and local Zakat committee chairman or his nominee at up to matric level and district Zakat committee chairman or his nominee at above matric level. For educational stipends for Madaris, only those which are duly registered with one of the five Madaris boards are facilitated after having been enlisted with provincial Zakat administration after the approval of Khyber Pakhtunkhwa Zakat and Ushr Council through signing of proper MoU between Zakat and Ushr Department and the Madrasa concerned.

Hospital treatment of higher amount is successively approved by higher-ups from Health Welfare Committee (up to Rs. 50,000), Chief Zakat Administrator (up to Rs. 100,000), Chairman Zakat and Ushr Council (up to Rs. 200,000) to Minister of Zakat and Ushr (up to Rs. 300,000). A committee of these officials decides for grants above this amount.

Health Welfare Committee at the level of each medical institution/hospital enlisted with provincial Zakat administration comprises chairman Khyber Pakhtunkhwa Zakat Council or

his nominee, medical superintendent/HD, chief pharmacist concerned and district Zakat officer. The first two are co-signatories and the last two are members.

#### 4.1.7.1. Identification of Beneficiaries: Issues and Problems

One of the biggest perceived problem is political interference at times. However, it has been reduced to a great deal now with second level head office verification.

Although there are deserving people, but they do not qualify due to limited funds. For disbursements, cash transfers are prioritized to the disabled people which require more urgent assistance. University scholarships are rare since there are multiple ways to finance education.

Political interference is one of the biggest perceived problems at times.

Health allowance is also given less importance after the launch and increased coverage of Sehat Card. Provision of healthcare assistance is based on first checking that whether it is already covered under Sehat Card or not. Disbursement regulations state that any patient getting medical assistance from Sehat Sahulat Card, Pakistan Bait-ul-Mal or any other resources shall not be entertained out of Zakat fund.

Due to the requirement of submitting more forms, local Zakat committees feel that some genuinely deserving applicants are denied even after their forms are submitted. People whose forms were submitted by local Zakat committees start to feel that it was the local committee which was at fault for their non-qualification.

Another important hurdle in identification of beneficiaries is reaching far-flung areas where the law and order situation and road networks are not exemplary. Increase in cost of travel is also a big hurdle.

The chairman and members of local Zakat committee work on voluntary basis. It is very hard for them to travel to far-flung areas to find deserving beneficiaries without any compensation and travel allowance. It is also very difficult since they are told that only a few forms will be eventually entertained and some submitted forms will nevertheless be rejected. By and large, local Zakat committee chairmen and members aired their grievance on this requirement of having to submit more forms while it is pre-known that at least half of these applications will be rejected.

Local Zakat committee members also showed concern that they do not have access to verify duplication from BISP records. Local Zakat committee does not have access to verification from BISP in screening at the moment.

#### 4.1.7.2. Selection of Beneficiaries: Issues and Problems

For educational stipends and health grant, only government schools, colleges and hospitals are usually entertained. Many of these schools and hospitals offer free or subsidized services. However, as per general perception, the quality of service is not up to the mark in most of these government-run institutions.



There is also variation in practices and preference among regions. Some districts reported that they only prefer special education schools to cater to the more neglected children.

All in all, while identifying, screening and approving beneficiaries, habitual beggars, government servants and relatives of local Zakat committee chairmen are not eligible and hence they are not selected. The Zakat Department screens the requests forwarded by local Zakat committees to determine eligibility. The approved beneficiaries are then provided with order cheque to ensure transfer of funds directly. ATMs or easypaisa are not utilized at the moment in KP province.

It was also learnt during focus group discussions that some good hospitals are sometimes reluctant to even take grants because of duplication of audit.

Support from Zakat funds in critical illness and injury is hard to get since the patient has to go to local Zakat committee chairman to determine Istehqaq (eligibility). In emergency cases where Mustahiq patient requiring emergency treatment is unable to produce Istehqaq certificate from local Zakat committee, any member of the KP Zakat and Ushr Council may also determine Istehqaq of such patient on the guarantee of some relative, friend or other reliable person. However, after emergency treatment, the beneficiary has to produce Istehqaq certificate within 30 days, failing which the Mustahiq will be blacklisted for any future assistance under the Zakat program.

On the other hand, disabled people also face problem in getting disability certificate. Their mobility is restricted because of their disability in the first place. Then, hospital committee meets after 15 days at particular hours in city areas. The three-member committee includes medical superintendent, social welfare officer and doctor. If they are absent, then no decision is taken.

It was reported by participants in the focus group discussion in one of the districts that BISP verification is done after cheque issuance in some cases. It wastes cheque, creates unnecessary hassle and complexity in audit and may even lead to underutilization of funds. However, the head office representative denied that this may have been the sole issue and even if it was, it would have been a very rare exception.

One informant in focus group discussion also shared the concern that if a computer operator is transferred, he still has the password and can enter data. After transfer postings, the password must be changed. Regarding this issue, the head office replied that this would have been a one-off event. Passwords are changed when a replacement officer takes over the duties of an outgoing officer.

#### 4.1.8. Disbursement Process

The beneficiaries who qualify for Guzara allowance get to know about their qualification success mostly from local Zakat committee chairman. The approved list is sometimes displayed in mosques. Local Zakat committee chairmen also inform beneficiaries themselves.

A person receiving funds in first instalment will not be deprived of the second six-monthly instalment during that year until and unless he/she expires, migrates to some other place, is proved as non-deserving for Zakat or refuses to receive assistance.

Disbursement is done through order cheque to facilitate disbursement of funds to those who do not have bank accounts. Cash payment is avoided as it may increase the chances of misappropriation of funds. That is why, neither the officers of Zakat Department nor the local Zakat committees have any role in direct cash disbursement.

The chairman and vice chairman in each local Zakat committee sign the order cheques in the name of beneficiaries who are qualified. In marriage assistance grants, crossed cheques are used instead of order cheques.

District Zakat office sends LZ-11 list (approved beneficiary list) to banks along with CNIC number of beneficiaries. As of now, there is no hotline, online tracking or SMS facility to inform about qualification and call for collection.

#### 4.1.8.1. Disbursement Process: Issues & Problems

Often, non-utilization is due to technical reasons like discrepancy or limited information in beneficiary record, delay in funds receipt or cheque not cashed in time due to illness or non-availability in area.

Since two times as many forms are required as compared to the actual beneficiaries who are entertained, those who do not get funds in final cut get dissatisfied and even accuse local Zakat committees. Local Zakat committee chairmen feel overburdened in submitting more applications and then having to face as many dissatisfied applicants as the approved applicants.

Only the head office has access to data from BISP. BISP check is done much later in the process, rather than as the first filter at the first point of contact. It should be done early as a first filter to avoid tedious work later (if applicant is ineligible).

Due to requirement of submitting more forms, some local Zakat committee chairmen who worked meticulously in determining Istehqaq resigned due to time and work pressure in performing this voluntary task and which creates a bad image in their locality eventually.

Some local Zakat committee chairmen also stated that this requirement of submitting two times as many forms as compared to the forms approved encourages less effort in determining Istehqaq. It was alleged by some informants in focus group discussions that some local Zakat committee chairmen submit bogus forms too just to fulfil the requirement.

However, the department's perspective is that asking for more forms makes the process more transparent and helps in achieving efficient targeting. It also helps in more targeted allocation and utilization of funds even if someone is deemed ineligible in verification.

#### 4.1.8.2. Issues Related to Bank

There were many hurdles cited by local Zakat committee chairmen in bank account opening. Banks know that such accounts will have low funds and activity. Hence, they take less interest in opening such accounts.

Banks charge statement fee, cheque book issuance fee and taxes on that like federal excise duty are also not exempted. Sometimes, balance in the account becomes low so that the last beneficiary cannot be entertained. In such a situation, the beneficiary or local Zakat committee chairman has to deposit the deficit to clear the last cheque.

The use of order cheques as a medium of disbursement requires physical visit during banking hours. There is significant shoe leather cost, especially in far-flung areas. In Waziristan region, there are hardly any branches of banks. People have to travel to the branch and then also need to go through tight security. In South Waziristan, there are very few branches and very tight security to enter bank branches.

The bank staff takes less interest as the accounts opened for Zakat have low funding and activity.

The staff is also uncooperative and rude, and asks for unnecessary documentation.

It was also reported by some local Zakat committee chairmen and beneficiaries as well that staff is rude and uncooperative. They ask for unnecessary documentat ion and tell the beneficiaries to either wait for a long time or come again. It was also shared by the beneficiaries that staff creates hurdles in formalities such as signatures not matching.

Since order cheques have a limited life, they expire by 31st July. If people are not in the area in the disbursement season, then they may lose out on getting cash assistance.

It was shared by an auditor in key informant interviews that sometimes not all bank branches have an updated list. Payment is not disbursed directly to the beneficiaries via district Zakat office. It creates time lag and possibility of discrepancy in the process. It was also learnt during the focus group discussions that easypaisa is utilized in Punjab, but not in KP.

If there are unused funds, they go back to the department, but only after local Zakat committee chairman and vice chairman sign the cheques. Else, there are issues at bank on recovery of that amount.

Another important concern shared by the district Zakat officer in one of the discussions was that district Zakat office does not have any discretion to utilize unused funds in disbursements. Due to this, some of the funds do not go to the beneficiaries in a timely manner.

#### 4.1.9. Auditing Process

Auditing is an important function to have an oversight of the entire process of Zakat management. It includes internal and external audit by Auditor General of Pakistan. Some

districts are audited annually and some are not audited for several years. Internal audit starts after disbursement is complete. External auditor usually performs audit on one-third of the data.

Internal audit usually relies on verification of documents. Physical visits are made if there is inquiry and complaint. Some auditors, due to their own keenness, carry out extensive physical audit as well. It also depends on how developed, large and secure the area is and what is the condition of the roads and law and order.

Earlier, there was divisional audit, but now audit is done district wise. There is also an annual Departmental Accounts Committee meeting to which auditors are also invited.

#### 4.1.9.1. Audit Scope

The audit's scope includes verification of Tamleek (Qabzat-ul-Wasool) in Guzara allowance, marriage assistance, educational stipends and other heads of allocation.

An important aspect of verification is checking beneficiary CNIC (verified from NADRA) and his/her signature (to be matched from NADRA) on LZ-11 register. Tallying cashbook (LZ-12, LZ-13) and bank statement is also part of audit.

It was shared by one auditor that hospital audit includes audit of tenders. In schools, attendance register and in Deeni Madaris, kitchen is checked to ascertain that the institution is run properly.

In determining eligibility, it is important to check disability certificate, death certificate and age (60 for senior citizens and 16 for orphans) of beneficiaries. Audit also involves inspecting that whether the departmental instructions, guidelines and allocation targets are fully complied with or not.

#### 4.1.9.2. Grievances of Audit Staff

Even though audit staff is hired on MBA Finance qualification, but they work on a fixed salary. There is no periodic increment, career progression and job security.

They are contractual and not part of the usual government grades. Since their salary is paid from Zakat fund, they fear that declining Zakat allocation to the province may create job insecurity and make it even more hard to expect increment.

The salary is not directly transferred in their account from the head office. The medium of cheque in salary disbursement delays payments. Salary is usually paid as arrears from July to October.

Auditors also do not get any travel allowance. Sometimes they have to buy cellular minutes and internet bandwidth at their own expenses. Almost all auditors shared this concern that their work is severely handicapped due to no travel and communications support.

#### 4.1.9.3. Problems in Audit Process

Auditors are not given any travel allowance or transport facility to conduct field visits. So, audit is mostly restricted to verification of records. It was also shared by one auditor that very limited time was given for audit process in the year 2022. Sometimes audit starts before disbursement in all heads had been completed. This defeats the purpose of audit.

Audit staff salary cheques and annual confidential report is forwarded by district Zakat officer and the auditors are supposed to audit him as well which creates clear conflict of interest.

Sometimes, local Zakat committees delay submission of data and are sometimes not available for explanation and inquiries. Since major activity is in Guzara allowance once in a year, there are idle labor hours. Some auditors also engage in other sources of complementing income when the audit activity of Guzara allowance is no longer ongoing.

#### 4.1.9.4. Common Audit Observations

A few auditors shared their confidential remarks in audit reports. Common audit observations cited in those reports revolved around the following issues:

- ❖ In the past, there were cases of local Zakat committee chairman going to bank and asking for a cut from the beneficiary.
- ❖ Sometimes the beneficiary does not have a contact number. So, local Zakat committee chairman gives his own number in for the record. This creates problems in telephone verification.
- ❖ In one case, a woman was given cheques three times in a single year.
- ❖ Bank staff sometimes, due to haste, do not verify beneficiaries properly from the list.
- ❖ Some cases of embezzlement and bribe were also reported in the past.
- ❖ In some places, there is no local Zakat committee and disbursement has been done through administrator for a long period of time.
- ❖ In some places, unutilized funds are not returned back through cheque by local Zakat committee chairman and vice chairman. Sometimes, a chairman resigns or is removed from chairmanship, but he does not come immediately to the bank or intimate for transferring his responsibility of signatory to new chairman.
- ❖ Local Zakat committee chairman taking more funds from the account than is allowed, i.e. Rs. 1,500.
- ❖ Local Zakat committee chairman taking funds for personal use even if within the allowed limit.
- ❖ Giving marriage assistance grant to a woman who is already married since long.
- ❖ Giving cheques to relatives of local Zakat committee chairman.
- ❖ Bank staff giving cheque without updated list.
- ❖ Giving Guzara allowance and marriage assistance in the same year to a person.
- ❖ Local Zakat committee not maintaining LZ-19 to the required numbers.

- ❖ CNIC missing or wrong entry.
- ❖ All payment withdrawn at once and local Zakat committee chairman giving funds on his own to beneficiaries.

## 4.2. Ushr Governance in Pakistan

In Pakistan, there is allowance of Ushr collection in the law, but the collection has been minimal in the past. In fact, whatever little Ushr collection was done after the introduction of Zakat and Ushr Ordinance, 1980, now even that much has stopped. Since inception, Ushr collection could not be materialized as per the potential, but later even efforts and administrative capacity to collect Ushr all but vanished.

There is hardly any Ushr collection in Pakistan right now. Local Zakat committees were expected to play a role in this matter. But, the voluntary workers in local Zakat committees with no power and authority were not able to collect or even exert any effort to engage in Ushr collection.

The institution of Ushr initially showed some promise. Local Zakat committees were majorly responsible for Ushr assessment and collection. However, they did not play their role effectively. Hence, the system of Ushr has been halted and the system of Zakat has also been scaled down and is now limited to Zakat collection at source from some financial instruments only.

Voluntary collection of Ushr cannot be expected to grow given the trust deficit between the government and landowners. Since there is agriculture income tax as well from the provinces, the landowners would not like to pay Ushr to the government as neither they will get tax rebate nor will they be exempted from agriculture income tax. Thus, they avoid paying both agriculture income tax as well as Ushr to the government.

Even the voluntary payment of Ushr privately is not very common. Many people do not know the rules of Ushr. They are not aware of the Nisab and what kinds of expenses are adjustable from the production value of crops.

### 4.2.1. Challenges in Ushr Collection

#### 4.2.1.1. Inadequate Collection

There is inadequate collection at the level of government. Even though the share of agriculture in national gross domestic product is 20%, but Ushr collection is almost nil. Since the government is not collecting direct taxes on farm income, it does not have extensive record of land holdings and produce of agriculturists. Lack of documentation and inappropriate administrative capacity to assess and collect Ushr has resulted in dormancy in Ushr collection.

Ushr collection in Pakistan is almost nonexistent given the trust deficit between the government and the landowners, incomplete land records and non-documentation of agricultural sector.

#### 4.2.1.2. Incomplete Land Records

The land in Pakistan is fragmented and there are small landowners. It increases complexity in assessment. There is lack of documentation of land as well as record of agricultural output. Besides, some farming is of subsistence nature for self needs. No revenue record system in many areas means that Ushr cannot be institutionalized easily. Efforts are underway to digitize land records and make use of GIS technology. Still the documentary infrastructure is weak. There are also significant differences between the demographic and socio-economic development status of different districts; some are very poor as compared to others.

#### 4.2.1.3. Agriculture Sector is Largely Undocumented

The agriculture sector is largely undocumented. Due to income tax exemption, much of the income is shown as agricultural income whereas it is not. The Mouza Census 2020 can be carefully studied to understand the dynamics of this sector, details of seasons, average pattern in yields and relation of land dynamics with yield.

#### 4.2.1.4. Rural Centric Production Zones with Limited Agricultural Marketing Infrastructure

Production takes place in suburban and rural areas in most cases. Agricultural marketing infrastructure is very poor. There are information asymmetries, market imperfections, practice of hoarding, and volatility in yields. Ascertaining landowner identity and yield is not easy.

From assessment to collection, agricultural infrastructure is very poor. Payment of Ushr in cash is possible when the farmer is able to sell in the market. There is a need for transparency in price determination and for eliminating the manipulating role of middlemen and market makers. Unless the farmer gets fair price for his yield as well as incentives for reporting true yield, it will be difficult for the government to allocate its weak and small administration for assessment of Ushr in the largely undeveloped and dispersed agricultural market.

### 4.3. Governance of Waqf in KP

Khyber Pakhtunkhwa Waqf Properties (Amendment) Act, 2020 governs the legal framework of Waqf in KP province. There are 35 districts in KP and at least 11 have Waqf properties. Auqaf and Religious Affairs Department is responsible for the management and control of Waqf properties including Masajid and Madrasas across the province. The Auqaf Department was established in 1949 with the aim to promote religious education, harmony among the public, looking after the needs of Auqaf Masajid, shrines and Madrasas. The department looks after generation of revenues from the Waqf properties.

### 4.3.1. Challenges in Waqf Administration

#### 4.3.1.1. Inefficiency in Generating Enough Revenues

The rents are not market based and Waqf property is not managed and invested properly. Apart from below-market value rents, property is sometimes sold at throwaway prices. There is a possibility of involvement of kickbacks in such cases.

Only the hold and rent dormant model is used with no active management. There are no specific governance and operational standards if a Waqf is to be actively managed.

#### 4.3.1.2. Risk of Appropriation

There have been cases of appropriation of land. Properties are also usurped by private land grabbers. Land grabbing results in loss of control as well as revenues. If Cash Waqf is introduced, it may have more risk given the governance issues. When even land is appropriated, it is hard to ensure that there is no misappropriation and misutilization of Cash Waqf capital.

#### Major challenges in the administration of Waqf:

- Lack of efficient management and revenue generation
- The law does not recognize Cash Waqf
- No periodic reporting/auditing
- No private corporate sector engagement
- No public-private partnership
- Usurpation of Waqf lands by private land grabbers

#### 4.3.1.3. No Provision in Law for Cash Waqf

Waqf law does not recognize Cash Waqf. Since almost half of the population is poor and only a handful of people in the elite segment have enough real estate endowments and the generosity to dedicate property for public welfare, private Waqf establishment is almost negligible.

Even those people who may potentially dedicate property for public welfare remain skeptical that after giving the ownership and controlling rights to the government's Waqf Department, the purpose for which Waqf property is dedicated may or may not be followed subsequently.

Cash collection requires a sound background check and licensing scheme to filter cash flows. A licensing regime with detailed requirements needs to be developed first before license to establish Cash Waqf can be allowed. Sound governance is also necessary. Majority of people do not have bank accounts and handling of currency is even more prone to risk of appropriation and misutilization as compared to the immovable property.

#### 4.3.1.4. No Significant Public-Private Partnership

There is no active intent to develop the Waqf lands into shopping complexes, markets and multi-storey apartments to increase the overall value of land as well as rental income. Without development, Waqf property is leased and depreciates over time. Scattered Waqf land also becomes a challenge when it comes to maintenance and dividing the Waqf land to create shops in the marketplace on Waqf land, apartments on plots, and so on.



Builders can be given the Waqf land on long-term lease to develop the land into apartments and marketplaces and then, more rental income can be generated. Such joint ventures and build, operate and transfer models are not being employed at the moment.

#### 4.3.1.5. No Orientation of Using Waqf for Social Protection

The Waqf Department currently works as a watchdog only. The main mandate is just guarding against illegal occupation and encroachment. The main focus is on maintenance. The budget details of expenditures also reflect that major expense heads refer to different kinds of maintenance and repair work. In key informant interviews at the Waqf Department in Punjab and KP, the only examples of use of Waqf in social protection were: some dispensaries, Madrasas and free food distribution on the occasion of Urs.

#### 4.3.1.6. No Reporting Standards

There is no periodic reporting of revenues and assets. There are no periodic audits on standardized parameters. Usually, the department is involved in dormant management, maintenance and protection of Waqf assets only.

#### 4.3.1.7. Complete Authority Vested with Chief Waqf Administrator

Complete authority is vested with Chief Waqf Administrator. The current regulatory framework is not inclusive for private corporate sector engagement. Public-private partnership models require flexibility in administration and sound governance.

Despite all powers resting with Chief Waqf Administrator, the cases of land appropriation and land grabbing do not give a promising picture about the soundness of governance.

## Appendix 4.1: Revisiting the Contemporary Application of Fiqh of Zakat and Waqf

In modern times, economic activities, modes of production, forms of production, production processes and the instruments to store various forms of financial and real wealth have changed. In the light of this, scholars have conducted research on finding the appropriate way to deal with these changes. In *Fiqh az-Zakat*, the most seminal work has been done by Allama Yusuf al-Qardawi.

As part of the study on exploring ways of institutionalizing, revitalizing and embedding Islamic social finance into the social protection policies and programs of the government, Institute of Policy Studies, Islamabad also sought formal opinion from Council of Islamic Ideology and other Dar-ul-Ifta in the country regarding certain aspects in jurisprudence of Zakat, Ushr and Waqf which require scholarly deliberation. In light of this, following is the summary of questions and their answers.

## Questions Related to Zakat and Ushr

### Questions Related to Nisab

#### Nisab of Ushr

- a) Respected Imam Abu Hanifa (R.A.) did not allow exemption in assessment of Ushr to be paid (Maulana Inam-ul-Haq Qasmi, 2006, Pg. 318 and Maulana Khalid Saifullah Rahmani, 2020, Vol 4, Pg. 393). Can this view be taken in modern times? This can help in checking Zakat evasion. For instance, if a person engages in production in such a way that each time, production is done inside the exemption limit of five Wasaq in a production cycle, then there will be no Ushr to be paid. By disallowing exemption, it will also help in assessment and monitoring from the regulatory and governance perspective.

**Answer:** When Zakat and Ushr Ordinance draft was being prepared, special efforts were made to reconcile the juristic opinions and reach conclusion where there is consensus. Majority of jurists are of the view that in light of Ahadith on Nisab of Ushr, it shall be used. Using the exemption limit is also convenient for the government to focus its attention on major productive activity.

- b) Should all means of production be exempted from Zakat? A small retailer is supposed to pay Zakat on unsold inventory at year-end while factory owners having millions and billions worth of productive machinery are asked to pay Zakat on few liquid assets subject to adjustment of debt. In modern banking system, bigger industrialists are able to take on bigger loans from banks. Their tradable inventory is easily sold to retailers and end users and they reinvest their earning partially or wholly in expansion and thus buying more productive capital as means of production. Referring to the views of Abu Zahrah, ‘Abd al-Wahhab Khallaf and ‘Abd al-Rahman Hasan, Allama Yusuf al-Qardawi writes in *Fiqh az-Zakat*: “Today’s plants and factories are the productive growing capital. Consequently, we conclude that craftsmen’s tools which the owner uses personally are exempted from Zakat because they are essential for his or her personal needs, but plants and machinery are subject to Zakat. No one can claim that by stating this we stand against the opinion of preceding jurists, since they never expressed an opinion on factories they never saw. If they had seen them, they would have given the same ruling. We are merely applying their standards and criteria to modern times (Pg. 245, Vol 1)”.

**Answer:** Means of production are exempted from Zakat. However, income earned from the means of production which is not consumed by the year-end, is subject to Zakat.

## Questions Related to Coverage

## Zakat and Ushr on Earned Income or Value Creating Activities

- a) Agricultural produce was a major source of earned income in olden times. Nowadays, there are other modes of earning income, such as rental income, capital gain on financial and real investments, consultancy income, services income, salaries, etc. Allama Yusuf al-Qardawi in his book *Fiqh az-Zakat* favors deduction at source of earned income as and when it is earned. Can this view be taken as it will be consistent with Anfaa Lil-Fuqara?

**Answer:** This view will compromise the principle of Hawlan-e-Haul. Zakat is levied not on income, but on certain forms of savings in the form of cash, gold, silver and tradable assets. Thus, if income from any source is unspent and kept in any of these above four asset forms, then Zakat will be levied once a year on the Zakat due date.

Zakat due date is the date on which one year passes after the person became Sahib-e-Nisab. For instance, if a person becomes Sahib-e-Nisab on 1st Ramadan, then he has to check on 1st Ramadan next year whether he still has Nisab level value of Zakatable wealth. If he has, then Zakat is due on him on 1st Ramadan.

- b) Should earned income be treated under Ushr or Zakat? If it can be treated under Ushr, then there is potential of higher resource redistribution from the haves to the have-nots and it will be consistent with Anfaa Lil-Fuqara? In contemporary view, rented buildings are only subject to Zakat on the rent value rather than entire value of investment by treating capital investment in real estate as means of earning income. In this case, if exemption is treated similarly as in Ushr, then can the rate of charge be Ushr as well given the fact that real estate investments and financial investments have intensive use of capital and not labor?

**Answer:** Ushr is applied on production from land. Other forms of production not arising from land are not subject to the rules of Ushr. Anfaa Lil-Fuqara is not the primary binding principle to determine the scope of Zakat and Ushr. It is a facilitating principle when deciding between two matters, both of which have separate legal basis independently. For instance, in Pakistan, Ulema recommend the use of silver Nisab as it will allow greater benefit to the poor. Silver Nisab is not introduced originally by the principle of Anfaa Lil-Fuqara. The principle is used to favor one of the two views, which is more beneficial for the poor.

- c) It is reported that during the rule of Umar bin Abdul Aziz (R.A.), salaries were given after deduction of Zakat (Musannaf Ibn Abi Shaibah, Vol. 4, Pg. 42-44). In the case of levying Zakat on leftover savings from earned income at year-end, the potential Zakat payer has an opportunity to either spend the surplus wealth or convert it into assets not subject to Zakat just before the Zakat due date. Allama Yusuf al-Qardawi writes in *Fiqh az-Zakat*: “This approach results in putting all the burden of Zakat on moderate or thrifty income earners and exempting extravagant spenders (Pg. 260, Vol 1)”. If earned

income is treated under Zakat, then is it possible to allow deduction at source as and when income is earned with or without subject to adjustment at year-end?

**Answer:** In the narrations which mention the deduction of Zakat at source from salaries, it is not mentioned that it is also not necessary to check for Hawlan-e-Haul. Since Hawlan-e-Haul is a basic requirement authenticated from other narrations, what can be inferred is that those employees were already Sahib-e-Nisab.

Hawlan-e-Haul is an Arabic term that literally means the passing of a year. In the context of Zakat, it refers to wealth being in a person's possession for the duration of a complete lunar year.

Therefore, if government deducts Zakat from salaries, it has to ensure that the person is Sahib-e-Nisab. The person should be allowed to adjust liabilities to determine true net Zakat liability. Finally, the condition of Hawlan-e-Haul shall be fulfilled. Since these adjustments are hard to be kept in perspective and the refund/adjustment process can be tedious, it is not advisable to follow the path of Zakat deduction from salaries at source.

### Questions Related to Zakat and Ushr on Industrial Production

Respected Imam Abu Hanifa (R.A.) opined that every produce from land is subject to Ushr while referring to a Hadith. Industrial production is also value-added production on produce from land. Since land which does not produce is not subject to Ushr, the basis of Ushr seems to be production rather than land. Our respected jurists exempted naturally occurring byproducts from Ushr which were not intended to be produced commercially. But, they applied Ushr on production which is obtained with a commercial motive. Thus, basis of Ushr seems to be commercially valuable production. This view would enable coverage of production from even vertical farming or bio-technology based agricultural production in contrived laboratory settings. Countries with intensive use of vertical farming and bio-technology based production are mostly high-income countries while the countries using traditional farming methods are low-income poorer countries.

Some experts have asked for extension of Ushr to fish farming. It is stated in Council of Islamic Ideology's Consolidated Recommendations on Islamic Economic System (1983):

“In the case of fish and other catch/produce of the sea and mineral produce, the rate suggested is 5% on consideration that the character of these productive activities is akin to cultivation on irrigated land, the produce of which is leviable at 5% (Pg. 151)”.

In modern economy, agriculture sector contributes less than 20% to the production. Major production value comes from production in the industrial and services sectors. Even agricultural production is now increasingly reliant and connected with industry as in agro-based industries. While the raw agricultural production gets very little value in exchange, the processed and value-added agricultural production in rice, wheat, food and textile industry gets much greater value in exchange in oligopolistic industries.

- a) In light of these contemporary realities in economic organization and structure, should Ushr be extended to production and earned income from value-creating activities in general? Doing this can eliminate the bias against farmers whose output is subject to Ushr, but the industrialists are exempted from similar charge on production and are also able to avoid Zakat if Zakat eligible assets are adjusted against liabilities. The net asset value of (Cash + Accounts Receivable + Investments + Inventory – Liabilities) in most cases is negative. Furthermore, in services sector, there is no tradable inventory which can be made subject to Zakat. Hence, by charging Ushr on agriculture while relying on Zakat at year-end on specific liquid assets in other sectors will result in most resources moving away primarily from the relatively less wealthy farmers while the large industrialists and services sector establishments will have an opportunity to pay much less with no tradable storable inventory and allowance to deduct debt against their cash, investments and accounts receivables balances.
- b) If the reasoning under ‘a’ is considered, then can we introduce a collection mechanism on the pattern of general sales tax like levy at the rate of 5% (Nisf Ushr) on the premise that production is with intensive use of both labor and capital in industrial establishments? Such sales taxes are levied on production without regard for expenses as well. In Ushr as well, the cost of production is not deducted (Maulana Inam-ul-Haq Qasmi, 2006, Pg. 315).
- c) Can earned income from financial investments where income is earned without providing labor effort be made subject to Ushr since only capital is employed to earn income? If yes, then deduction at source can enhance potential resource redistribution as well as ease the assessment and collection. Presently, the government also relies heavily on deduction-at-source based withholding taxation for its ease of collection with minimal chances of evasion.

**Answer:** Ushr is applied on produce from land. Zakat is applicable on businesses as well. However, condition of Hawlan-e-Haul shall be observed. It is not necessary that each and every asset shall be in ownership for one year. Only passage of one year since becoming Sahib-e-Nisab is required. Regarding liabilities, it is recommended that only the current portion of liabilities shall be allowed to subtract against Zakatable value of wealth.

Zakat should not be looked at as a form of taxation. For genuine welfare needs, government is allowed to collect taxes to meet its other needs.

#### Questions Related to Zakat on Corporations

- a) The Council of Islamic Ideology has recommended in the past to avoid double taxation. Should the corporation be regarded as separate juristic person? If yes, then is there a possibility of taxing corporations and shareholders separately?
- b) If answer to (a) above favors Zakat on shareholders separately, then is it possible to introduce measurable indicators to determine Zakat base? Currently, it is suggested that

if the intention is to earn dividend with long-term investment horizon, then Zakat is to be on Zakat eligible assets in the corporation subject to adjustment of debt. But, if the intention is to buy and sell on short-term basis to get capital gain, then whole value of investment in stocks is Zakat eligible. Since intention is hard to measure and changes over time, if holding period is introduced instead, it can ease in assessment and collection. Currently, the government has introduced a tiered capital gains tax which varies as per holding period of investment. Can such a mechanism be introduced as well in Zakat on shareholders?

- i. If shareholders are privately held responsible to pay Zakat, then can they be exempted from Zakat if they hold onto investment for a longer period? In that case, the Zakat is required to be paid on Zakat eligible assets only subject to adjustment of short-term debt. This levy can be charged from corporations. The issue of Nisab can be mitigated by the reasoning that shares are combined to determine Zakat eligibility for corporation as one unit, as favored by respected Imam Shafaie (R.A.). Mufti Inam-ul-Haq Qasmi, who has compiled encyclopedia on Fatawa on Zakat, had also stated that it is allowed to pay Zakat jointly or by individual shareholders in private capacity (Qasmi, 2006, Pg. 378 and 298).
- ii. If reasoning in point (i) is taken then, is it possible to introduce Ushr on capital gain (earned income) on the premise that only capital is employed to earn capital gain?

**Answer:** Imam Shafaie (R.A.) allows aggregating wealth in a joint enterprise to determine Zakat. However, Hanafi scholars have a different view. Shareholding of each individual can be known. Scholars recommend treating shares as a tradable asset if the motive of investment is capital gain from trading. But, if the objective is to engage in long-term investment and receive dividends, then net Zakat value shall be computed by counting the value of Zakatable assets minus the allowable liabilities that can be deducted. Then, each individual can pay Zakat by himself/herself. Since in the former case, capital gain for each person will vary, it is not easy to ensure Hawlan-e-Haul in collective Zakat deduction at source.

### Questions Related to Exemptions

#### Zakat on Convertible to Cash Assets to Disallow Zakat Evasion

- a) Respected Imam Shafaie (R.A.) disallows deduction of debt to determine Zakat base. Respected scholar Mufti Taqi Usmani restricts it to current liabilities and those which are undertaken against purchase of Zakat eligible assets. Given the debt-financed large businesses in modern economies, which view is suitable in modern economy keeping in perspective Anfaa Lil-Fuqara? Respected scholar Mufti Taqi Usmani has shared the view previously that only such debts be adjustable if taken to acquire Zakat eligible assets, such as inventory (Islam Aur Jadeed Maishat-o-Tijarat, Pg. 94). Maulana Khalid Saifullah Rahmani (2007) in his compendium Qamoos-ul-Fiqh writes that only the current portion of long-term debt which is due in current period is adjustable and not

the whole value of a long-term debt, which is spread over several years. If this view is taken, then can Zakat be deducted at the level of corporation requiring no further payment from the individuals?

**Answer:** Only the current portion of liabilities due in current year shall be adjusted against Zakatable value of assets.

#### Zakat Eligible Assets and Nature of Holding

- a) If intention is made the basis of determining Zakat eligibility, then assessment and monitoring will become problematic. Is it allowed to use some measurable indicators, such as holding period?

**Answer:** Zakat is a religious obligation. It is first and foremost an Ibadah. Every Muslim is expected to fulfil this responsibility. If Zakat is due, but if a person only avoids it by wrong intention, then it is a serious sin. The government, if required, can investigate true value of Zakat and Ushr liability if it deems that the person has misrepresented facts.

- b) Gain on sale within a short-term holding period will be treated as earned income and will be subject to deduction at source. If investment in real estate is made for capital gain or rental income, can both be regarded as earned income (rental income and capital gain)? If yes, then is it possible to treat them under Ushr which is deducted at source on the premise that real estate investments are made with capital and without labor. Will this be preferable from Anfaa Lil-Fuqara, distributive justice (by ensuring equal treatment to similar assets and productive activities and enterprises which seek earned income) and avoiding concentration of wealth within the rich (Al-Hashr, verse 7).

**Answer:** Zakat is only on that part of income of Sahib-e-Nisab which is kept in cash, gold, silver or tradable asset on the day when Zakat is due. Zakat is due once a year. Hence, deduction at source would compromise Hawlan-e-Haul and will also not allow the person to determine what is the unused income at Zakat due date if it is already deducted at source and not available for consumption.

#### Questions Related to Zakat on Personal Assets beyond Zaruriyyah

Allama Yusuf al-Qardawi contends that nowadays, wealth is stored in many forms. He favors determining an average standard of living and then subjecting asset and wealth beyond needs under Zakat. For instance, if a person owns multiple houses and multiple modes of transport, then, beyond his needs, the extra wealth stored in real estate and means of transport shall be subject to Zakat. Ibn Hamid, a Hanbalite, says that “if jewelry is below one thousand mithqal, it is lawful. Once it reaches that much, it becomes unlawful and consequently subject to Zakat”. Can this view be taken keeping in view promotion of Anfaa Lil-Fuqara, discouragement of Israf, ensuring distributive justice and avoiding concentration of wealth within the rich (Al Hashr, verse 7)?

**Answer:** Assets in personal use other than gold and silver are exempted from Zakat. If asset is purchased for the intention of sale for profit, then such asset is Zakatable. However, if this intention changes during the year or on the day of Zakat due or if this intention was not there from the beginning, then, the asset is not Zakatable.

### Questions Related to Extending the Zakat Net for Consistency

Verse 103 of Chapter Tawba asks Prophet Muhammad (PBUH) ‘Take from their wealth ‘O Prophet’ charity to purify and bless them...’. If Zakat purifies wealth, then would it not be consistent that it will purify all surplus wealth. Zakat has been extended to currency, financial assets and buffalo by inferring from the ‘Nass’ and extending the ruling. Hazrat Umar (rta), Hazrat Usman (rta) and Fuqaha in the past have performed Ijtihad to extend Zakat to contemporary assets and modes of commercial production. Allama Yusuf al-Qardawi in his book *Fiqh az-Zakat* (Pg. 63, Vol 1) argues that the word ‘Mal’ used in the Qur’an and Ahadith is general and can be extended to incorporate contemporary forms of wealth in its meanings.

Most wealth is concentrated with large corporations, industrialists and property owners. However, they remain outside of Zakat and Ushr net if they hold these assets without intention to sale and if such assets represent means of production. If the objective is to purify wealth, would the forms of wealth having high store value and exchange value not come under Zakat? For example, ornaments, luxurious cars and spacious homes beyond regular personal needs as argued by Allama Yusuf al-Qardawi in his book *Fiqh az-Zakat* (Pg. 63 and 66, Vol 1). Respected Imam Shatibi (R.A.) has devised needs into Zaruriyyah, Hajiyyah and Tahsiniyyah.

- a) Would it be permissible to subject assets beyond Hajiyyah Asli to Zakat as they form significant part of many people’s wealth? Can an average living standard be devised and used in assessing Zakat on wealth beyond Hajiyyah Asli? Is it possible to subject Mal-e-Mutaqawwum convertible in Nuqud to Zakat which is held in ownership beyond Hajiyyah Asli?
- b) Several Ahadith refer to surplus livestock and ornaments cursing and punishing the holder on Judgment Day (Sahih Muslim, Book of Zakat, Hadith No. 2166). One Hadith says that a woman who had bangles was warned to give Zakat on them, else, in punishment, one may be given bangles of fire to wear on Judgment Day (Sunan Nisai, Book of Zakat, Hadith No. 2479). Is it considerable that those Ahadith were discouraging hoarding wealth and not paying Zakat on them by referring to the common forms of wealth prevalent during the time of Prophet Muhammad (PBUH)? Does the concept of Adl demand that hoarding wealth in the form of luxurious cars and spacious homes beyond needs shall be subject to similar attitude and tendency that is discouraged and condemned in Ahadith?

**Answer:** Zakat is levied on assets with the feature of growth potential. As per Islamic jurisprudence, Zakat is due on cash, money kept at bank, receivables, financial investments, money kept in insurance companies, gold, silver and all tradable assets, either real, financial or



intangible. Only assets in personal use like home, furniture, means of transport, etc. are exempted from Zakat.

### Questions Related to Administration

#### Distinction of Amwal-e-Zahira and Amwal-e-Batina

- a) The Qur'an in verse 103 of Chapter Tawba says to Prophet Muhammad (PBUH): "Take from their wealth 'O Prophet' charity to purify and bless them...". Hazrat Abu Bakar (rta) was also adamant on taking Zakat from the wealth of people and did not allow private disbursement as long as the Muslim state had capacity to keep the collection centralized. Maulana Khalid Saifullah Rahmani (2007) in his compendium *Qamoos-ul-Fiqh* writes that as Muslim state grew geographically and as living standards also improved with multiple sources of revenues becoming available to the Muslim state, the distinction was made between Amwal-e-Zahira and Amwal-e-Batina. Was it an administrative decision?
- b) The assets which were Amwal-e-Zahira of past like livestock are more difficult to inspect than money in bank, mobile and online accounts as well as money invested in capital markets, commodity markets, real estate, vehicles, and businesses. The Amwal-e-Batina of past are more easily revealed. Given the high state of poverty in the Muslim world and increasing decline in the level of integrity and morals, if blockchain and other technologies can be used to monitor wealth effectively, is it allowed to increase the net of assets on which government can collect Zakat?

**Answer:** It was an administrative decision. With advancement in technology and documentation, it can be revisited to affirm that which asset forms are easily traceable to their owners and hence Zakat can be levied on them.

#### Averaging Fluctuating Zakatable Assets

In Council of Islamic Ideology's Consolidated Recommendations for Islamic Economic System (1983, Pg. 151), a recommendation from a panel is stated which allows averaging balance for assessment of highly fluctuating Zakat eligible assets, such as balance in account and tradable inventory. Economic advantages of averaging include ease in assessment and ensuring that Zakat is not avoided or evaded. Using average balance is also employed by Islamic banks in determining profits for the depositor in horizontal distribution of profits among the depositors.

The Council of Islamic Ideology allows averaging balance for assessment of highly fluctuating Zakat eligible assets.

In the case of Ushr, if average productivity yield in an area is used to determine Ushr liability, then it can help in assessment by applying the average yield to a particular cropping area whose size is easily measurable, but its yield is not measurable at the time of harvest or afterwards. Sometimes, even the owner is not confirmed about actual productivity and may keep no

documentation. In allowing for exceptions, an appeal or review mechanism can be introduced which is to be handled by a third party. It will have nominal fees, which will be refunded after the farmer is able to provide evidence that his crop was lower than average or was lost in some catastrophic event. It is also possible to charge Ushr or Nisf Ushr at the point of sale if government is monopsony in agricultural commodities buying. Can the average productivity in an area applied to a particular cropland area be used to assess Ushr to be paid and will it be consistent with the concept in Islamic sources which urge the Aamileen to take neither the best nor the poor, but average yield?

**Answer:** It is not advisable to apply an average on all fields. It can lead to inexact measurement. The person who is supposed to pay Ushr would also not want to pay less Ushr as it will be a sin. The government should improve its system of assessment and then transparent disbursement of *Mustaheqeen* to build trust so that people have no hesitation in revealing their true yield.

### Questions Related to Allocation

#### Using Zakat on Public Goods

In current times, welfare for poor is organized in an institutional setting whereby, they are provided with food, water, sanitation and support services like health and skills-based education to enable them to exit poverty. Some of these services originate from a public good or common property resource, such as water filtration plant, anti-malaria sprays, public schools, public hospitals, public libraries and public transport, to name a few.

- a) Is it possible to use *Wakalah-bil-Qabz* in collecting and *Wakalah-bil-Sarf* in allocation of Zakat where the institution providing welfare services to the poor is made *Wakeel* to receive and allocate Zakat on behalf of *Mustaheqeen* on their welfare with approval?
- b) Is it allowed also in cases where ownership is not confined privately, but services are provided to the *Mustahiqeen* from the infrastructure that is built from the Zakat funds? In this regard, Imam al-Razi (R.A.) writes that ‘to’ indicates ownership, while ‘in’ connotes the purpose of the spending in verse 60 of Chapter Tawba. Allama Yusuf al-Qardawi argues in *Fiqh az-Zakat* that Shari’ah requires that Zakat funds are for the *Mustahiqeen*. They can be spent on their welfare. Ibn-e-Munir in *Al-Intisaf*, a footnote of ‘*Kishaf*’, writes ‘Only the view that Zakat shall be spent for the *Mustaheqeen*’ is content with the word ‘*fi*’ as well as ‘*Laam*’ simultaneously. Please shed light on this.

**Answer:** *Tamleek* is regarded as a ‘*Rukn*’ (pillar) of Zakat among jurists. It also ensures that ownership of Zakat goes to the *Mustahiqeen*. The expenses of welfare activities and institutions can be managed through *Sadqat-e-Nafila* and by taxes in the case of government.

### Questions Related to Waqf

**Question:** Consumable assets give their benefit when they are spent. In today’s era, currency is used as a means of exchange and is also stored as wealth. Can a person endow (*Waqf*)

currency? How can this be possible? Can Waqf of cash be allowed if the cash is invested and only the income is used for charitable purposes?

**Answer:** According to the viewpoint of the contemporary Hanafi scholars, Waqf al-Naqud is permissible. However, the method of benefiting from Waqf al-Naqud will be to keep the Waqf's original amount intact and make a legitimate investment. Income earned from investment can be spent on the beneficiaries keeping in mind the conditions of the Waqf.

**Question:** It is considered that Waqif's deed is like Shari'ah ruling. Sometimes, circumstances change and there is need for change in the Waqf assets or its benefits. For instance, a Waqf was made to provide water in a locality. After sometime, the water problem is solved and now there is surplus water. Can some other need of the locality be served from the Waqf?

Can the Qazi or the government suggest any change considering the collective benefit? Is it possible to put a clause in the Waqf deed that the judge or the government can change the use of the Waqf considering the expediency and collective benefit? Can this potential problem be resolved if Waqf deed with this clause is signed by the Waqif with informed consent?

**Answer:** The ruling on the exchange of Waqf is that we need to look at whether the Waqif has given permission of exchange or not.

When the Waqif has permitted exchange, then the exchange of the Waqf is permissible, whether it is possible to benefit from it in the relevant consumption or not.

But, when the Waqif has not permitted exchange while dedicating it, then in this case if it is possible to get some benefit from the Waqf in the relevant consumption, then it cannot be changed simply on the basis of potential greater benefit. But, if the benefit from the Waqf asset ends, then it is permissible to replace it with the permission of the Qazi/court. It is also permissible to include a clause regarding the permission of substitution of Waqf asset in the documents.

**Question:** Can it be inferred from the opinion of Imam Abu Hanifa (R.A.) that temporary Waqf is also allowed if the Waqif endows an asset for a certain period of time. Is it possible for people to provide interest-free loans for a short period of time with a charitable motive?

**Answer:** There is no concept of temporary endowment for a specific period, because the purpose of endowment is to get benefit from something permanently. Qard without Riba is allowed and it is one of the charitable acts. It is also possible to make investments and dedicate profits from the investment to some charitable cause.

### Questions Related to Zakat-Based Qard al-Hasan

#### Questions:

Can Zakat be given as Qard al-Hasan to organizations, such as Akhuwat?

For instance, when the loan is returned, then it is given to another deserving person on a rolling basis. In this case, the beneficial ownership is with Akhuwat on the behalf of its beneficiaries.

If it cannot be allowed due to the condition of Tamleek, then is it possible that Zakat received is given as loan for some short period of time and after three or four loan cycles, a Mustahiq-e-Zakat is made the permanent owner of the Zakat amount. This way Tamleek is ensured and for some short period of time, people can benefit from the revolving Qard al-Hasan.

If Akhuwat is entrusted with the authority to collect Zakat from the government, can it collect some money for itself with the permission of the government as an agent?

**Answer:**

It should be noted that any charitable institution or organization, even if it is registered with the government and the government has also allowed it to collect Zakat and charity, still it is not under the command of the Amil (agent), because the agent is basically the ruler's deputy for the collection of Zakat. A person becomes agent only through regular appointment by Imam al-Muslimin.

Charitable institutions are not considered as 'Amalin' by the government, nor are they under their jurisdiction. Therefore, no charitable organization can claim itself to be 'Amil' in the collection of Zakat.

When these institutions act as trustee on behalf of the Zakat payers, they receive money and pay Zakat to Mustaheqeen. It is necessary to make a deserving person owner of the Zakat amount.

Since the charitable institution is not the agent of the government, but the agent on behalf of the Zakat payers, the obligation of Tamleek is not fulfilled by taking possession of the Zakat money. Also, this money is a trust with him and his possession is considered as the possession of a trust, and according to Shari'ah, the trust money cannot be given as a loan by the trustee himself because this is tantamount to a breach of trust.

Therefore, there should be no delay in delivering Zakat amounts to those who are entitled to Zakat, because delaying without any reasonable excuse is not without sin. Also, if the amount of Zakat is wasted without being delivered to the beneficiaries, the Zakat will remain on the person responsible. Although giving a loan is a good and 'Mustahab' act, Shari'ah does not allow the give-up or postponement of an obligation (Farz) for the sake of a good 'Mustahab' deed, so institutions should avoid giving the amount of Zakat on Qard al-Hasan.

However, if a Muzakki, while giving the amount of Zakat to the organization, explicitly allows that, for example, it is permissible to give this amount as Qard al-Hasan for such a period, and after that, give this amount as Zakat to the deserving, then it can be given as a loan according to this permission. This is when Zakat is paid in advance.

However, if the Zakat is currently due, i.e. if it is the previous year's Zakat, then the payment of Zakat should not be delayed for no reason. For example, if someone gives Rs. 200,000 with the intention of advance Zakat and at the same time gives permission to give it as a loan, then some amount could be given as a loan and when Zakat becomes due, the amount should be given as Zakat to the beneficiaries.

The mentioned charitable institution is not under the command of the agent, so it is not permissible to take wages from the amount of Zakat as an agent.

### References

Al-Razi, F.A.D. (1980). *Al-Tafsir al-Kabir*. Beirut: Dar Ihya'al-Turat al-Arabi.

Council of Islamic Ideology (1980). *Consolidated Recommendations on Islamization of Economic System in Pakistan*. Islamabad: Council of Islamic Ideology.

Qardawi, Y. (1984). *Fiqh-uz-Zakat*. Jeddah: Centre for Research in Islamic Economics, King Abdul Aziz University.

Qasmi, I.H. (2006). *Zakat ke Masail ka Encyclopaedia*. Karachi: Bait-ul-Ammar Karachi.

Rahmani, K.S. (2020). *Qamoos-ul-Fiqh*. Karachi: Zam Zam Publishers.

Usmani, M.T. (1983). *Islam Aur Jadeed Maeshat-o-Tijarat*. Karachi: Idarat-ul-Maarif.

## Chapter 5

# International Best Practices in Islamic Social Finance

### 5.1. Overview of Zakat in Malaysia

#### 5.1.1. Regulatory and Governance Framework of Zakat

The Federal Constitution has listed Zakat under state jurisdiction. All states in Malaysia have allocated matters related to Zakat affairs under acts or enactments in their respective states or are placed under specific enactments about Zakat.

Malaysia has 14 states and three federal territories. Each state has its own Zakat system and policy. In this sense, the system is decentralized to the state level. Each state has State Islamic Religious Councils (SIRCs) which look after the administration of Zakat and Auqaf. The administration of each Zakat institution is subject to the authority of the SIRCs. Each state has a different Zakat administration model. SIRCs directly report to the Sultan who holds the stature of Ulul-Amr. Succession of Sultan from one to another follows hereditary chain.

All fourteen states in Malaysia have their own Zakat systems and policies.

There are specific laws and enactments which regulate the Zakat system; however, Fatwas of the SIRCs have an important role in running the affairs of Zakat as well.

Each state collects Zakat on behalf of the Islamic Religious Council. There is no central collection and distribution. However, there are agencies known as Jabatan Wakaf, Zakat dan Haji (JAWHAR) responsible for planning, implementing, monitoring, and coordinating the development of Waqf, Zakat, Mal and Hajj/Umrah institutions to function more effectively in the socio-economic development of the Ummah.

#### 5.1.2. Scale of Zakat Collection and Disbursement

In 2020, the total Zakat collection in Malaysia was recorded at RM 3.5 billion. Out of that, Zakat collected in federal territories was around RM 821 million in 2021. It increased from RM 756 million recorded in 2020. In 2022, Zakat collection in federal territories is estimated to reach RM 900 million. Kedah State alone collected Zakat of RM 233 million in 2021.

The total Zakat collection in federal territories is illustrated in Table 7 below:

**Table 7: Zakat Collection in Federal Territories in 2020 and 2021**

No	TYPE OF ZAKAT	COLLECTION (RM)		NUMBER OF ZAKAT PAYERS	
		2021	2020	2021	2020
1	Income	553,297,642	511,309,117	193,456	184,170
2	Business	123,087,686	122,947,206	5,326	4,583
3	Savings	82,618,805	63,047,112	30,660	21,996
4	Mal (Harta)	51,253,956	49,102,156	6,103	6,374
5	Qadha	1,069,343	664,100	1,012	627
6	Others	10,412,917	8,935,228	195,682	218,496
	<b>Total</b>	<b>821,740,349</b>	<b>756,004,919</b>	<b>432,239</b>	<b>436,246</b>

Out of RM 821 million Zakat collected in 2021, around RM 353 million was paid by males, RM 232 million by females and businesses paid RM 113 million. Around RM 123 million Zakat was collected without knowing the gender identity. The number of Zakat payers included almost equal number of males and females.

The expense break-up for 2021 is shown in Table 8 below. Total direct costs were only about 2.1% of total collection while total indirect costs were around 3.59% of total collection. These direct and indirect costs together were lower than the 6.25% of total collection, which is the upper limit for Amil Budget from Zakat collection.

**Table 8: Expense Break-up of Zakat Administration in Federal Territories**

	Jan – May 2022 (RM)	Jan-May 2021 (RM)	Jan-Dec 2021 (RM)
<b>Direct Cost</b>			
<b>Marketing Cost</b>	3,630,152	2665558	8,995,326
<b>Operation Officer Cost</b>	3,921,837	3579059	8,286,362
<b>Counter Rental</b>	90,765	89,878	210,872
<i>Total Direct Costs</i>	7,642,754	6,334,495	17,492,560
<b>Indirect Cost</b>			
<b>Salary/Allowance/KWSP/PERKESO</b>	4,119,810	4,036,645	9,775,126
<b>Bonus</b>	-	1,497,183	3,360,191
<b>Human Resource Training</b>	1,721,053	1,334,469	2,868,634
<b>Management Expenses</b>	3,891,477	3,798,203	13,477,006
<i>Total Indirect Costs</i>	9,732,340	10,666,500	29,480,957

### 5.1.3. Tax Incentives on Zakat

One of the advantages of paying Zakat in Malaysia is that it allows a rebate in annual income tax. A tax refund is a reduction in the income tax a person has to pay, unlike a tax relief, which reduces the amount of taxable income only. The limit on the amount of tax refund a person can claim for Zakat is subject to the maximum tax charged. Paying Zakat can help people significantly reduce the amount of income tax that needs to be paid, and this reduction can sometimes be enough to reduce the income tax to RM 0.

In Malaysia, for salaried employees, there is 100% tax rebate facility. It means that if a person has paid Zakat of RM 1,000 and the person is required to pay income tax of RM 3,000; then, RM 1,000 Zakat paid can be directly adjusted in tax liability. However, this incentive is only available if Zakat is paid to the government. Hence, it creates an incentive for people to not only pay Zakat, but also to pay it to the government to get the tax rebate.

For government employees in Kedah, it is mandatory to pay Zakat which is deducted at source on salaries.

The Zakat payment receipt must be kept by the taxpayer for seven years as set forth under Section 82 of the Income Tax Act (ITA), 1967.

#### 5.1.4. Zakat on Business

There is Zakat on business in Malaysia. As discussed earlier, rebate for Zakat paid by businesses is capped at 2.5% of annual aggregate income. On tea and palm oil plantations, Zakat on business is applied. Zakat is paid on net income after sale and not on produce.

Ushr rules are only applied on food items like rice. Nisab on rice is approximately 1,000 kg which equals five Wasaq. Ushr is collected in terms of money rather than in kind.

When businesses pay voluntary Zakat, Kedah State has a scheme of giving a special logo which can be used in packaging and labeling of the product. It improves the image of business as well in society. It shows to people that these businesses are contributing to philanthropy by directing their Zakat payments through Lembaga Zakat Negeri Kedah.

On businesses, the tax rebate is capped at 2.5% of annual aggregate income. For instance, if a business has paid Zakat of RM 100,000 on annual aggregate income of RM 1,000,000, then Zakat rebate will be capped at RM 25,000, i.e. 2.5% of annual aggregate income.

#### 5.1.5. Zakat Collection

##### 5.1.5.1. Awareness Campaigns

Creating awareness and facilitating Zakat payment is one of the core functions of Zakat department. Awareness seminars are organized from time to time. Imams as Amil Assistant also help people in answering their queries on Zakat calculation.

Community programs are organized to create awareness as well as urgency among the masses to pay compulsory Zakat as a form of Ibadah. Ulema in Council also issue Fatwa to help people pay their Zakat on new forms of income and wealth, such as Zakat on digital assets. For the removal of misperceptions about Zakat department, if any, Lembaga Zakat Negeri Kedah uses the influence of Ulema in society. The staff of Zakat department visits them and requests them to create awareness among people about the importance of paying obligatory Zakat.



The department provides honorarium to such Ulema as well. Some proportion of the Zakat fund collected with the effort of such people are paid to them under the head of Amileen Zakat. The permission for allocation for such purpose is taken from religious council via Fatwa.

The department of Zakat provides help in the assessment of Zakat in various states. Anyone can call for some clarification or make an appointment with the experts. If people ask very technical questions, then they are referred to knowledgeable people; otherwise, the common and routine questions are responded immediately.

Pusat Pungutan Zakat MAIWP in particular has multiple ways of engaging people in creating awareness, urgency and sensitivity about obligatory Zakat payment. There is a hotline number where the trained staff and Mufti can answer queries.

E-Calculators on website and mobile applications can help in Zakat calculation. They are prepared in local language with smart inputs and in-built formulas so that people can calculate how much Zakat they are supposed to pay. If people come to Pusat Pungutan Zakat MAIWP, trained staff is there to assist them in calculating Zakat. These campaigns and efforts are very important as still, an estimated two-third of the population is not paying Zakat, partly because of lack of awareness about how much Zakat to pay and when it is compulsory to pay. People who participate in awareness seminars and events are encouraged to give Dawah about compulsory payment of Zakat in their social networks so that more and more people become Zakat payers.

#### 5.1.5.2. Collection Methods

Collection is facilitated by collecting agents and Amil Assistants. Kedah State has more than 700 collecting agents.

There are collection centers at local and district level. Any person can visit the collection centers and deposit Zakat. In addition to that, Zakat can be paid to the designated accounts of

Federal Zakat Department has five deposit vans equipped with all necessary tools for Zakat collection. The van can be called for Zakat collection to specific areas.

Zakat departments online. Various departments such as post offices and banks also offer services for the collection of Zakat.

In the federal area, a special collection van visits people for depositing Zakat. There are five deposit vans with federal Zakat department and these are well-equipped with the necessary tools such as computer, printer and Wi-Fi connection. The vans are also available on call and the organizer of some large gathering can invite the van, which reaches them for the collection of Zakat. Usually, organizations call the vans to run campaigns among their staff and administration.

People are not encouraged to pay Zakat privately. The decision of the Syarak Consultative Committee of the Federal Territories, which met on July 31, 2018, has explained that Zakat

must be paid in the state where a person works, no matter where he stays. Thus, individuals and businesses are encouraged to pay Zakat to Zakat institutions.

Section 16 (b) of the Syariah Criminal Offenses Act (Federal Territory), 1997 (Act 559) clearly allocates authority to the Council or its representatives to collect Zakat. This means that a person who pays Zakat or Fitrah through an Amil who is not appointed by the Council commits an offense under Section 16 (b) and can be punished if convicted.

Since there is no rebate unless Zakat is paid to the government's Zakat department, people have incentive to pay to the government and get tax rebate. People who want to pay their Zakat to family and institutions, they can also opt for Wakalah program. They are allowed to give instructions of Zakat payment for up to 50% to the Zakat department. This much portion of Zakat would be provided to the designated beneficiaries as identified by the Muzakki. For instance, in 2020, out of total Zakat collection of RM 821 million, around RM 120 million was returned back to people so that Zakat is paid to the identified beneficiaries.

Private institutions who wish to collect Zakat can become agents in the Wakeel program of Pusat Pungutan Zakat MAIWP. Private institutions are allowed to collect Zakat only after being officially appointed as Zakat collection agents. In the practice of MAIWP, disbursement of Zakat funds has also been allocated to institutions on a case-to-case basis. This usually happens in aid to NGOs that manage people with special needs. PPZ gives compensation to appointed and approved Wakeel, such as NGOs from the head of 12.5% Zakat funds earmarked for Aamileen.

As per the current legal framework, it is not compulsory by law to pay Zakat to the government. There is encouragement and incentives, but no strict legal compulsion. Changes in this legal framework have been tabled before legislators, but not approved yet.

However, if people give consent, Zakat can be deducted at source through standing instructions. Pusat Pungutan Zakat MAIWP has a monthly Zakat payment plan wherein people can commit to pay a certain amount of their choice monthly to Pusat Pungutan Zakat MAIWP. The frequency and amount can be changed as well by people afterwards if there is need. This helps people in budgeting their Zakat over the course of the year and avoid non-payment due to forgetfulness or because of overspending.

### 5.1.6. Zakat Disbursement

#### 5.1.6.1. Eligibility Checks

In some states like Kedah, Amil Assistants perform the eligibility check to determine eligibility of the applicant for receiving Zakat. Amil Assistant is imam of a mosque. There are 584 mosques in Kedah State and one Amil Assistant serves from each mosque. Desirous applicants contact the Amil Assistant who is accessible to them in the mosque as the imam. The mosque imams are appointed by the Sultan and they are professionally paid for their services by the SIRC.

The assistance of imam is taken for the purpose of Zakat collection, public awareness, and Zakat distribution. They motivate people for paying Zakat and help in double checking the information provided by the applicants of Zakat. Imams also help the needy people in filling the form. They also submit their recommendations in favor of the applicants; however, the final approval is made officially at district level, which recommends the names to the headquarter.

The department of Zakat has incentivized such assistance and some fraction of the collected Zakat is returned to the same mosque for helping the needy people. Likewise, some fraction of the collected Zakat is paid to the imam or his designated person under the heading of Amileen Zakat. Imams also help in the distribution of food packages from the food bank of the mosque. The food items for the food bank are provided by the Zakat department.

Amil Assistant can refuse an application if he deems the applicant to be not eligible. Eligibility is checked on Hadd-ul-Kifayah, i.e. limit of what amount will be sufficient to meet the real needs of the applicant.

Hadd-ul-Kifayah is like a poverty line derived from measuring the value of basic needs. Different states have their own Hadd-ul-Kifayah forms and details. Hadd-ul-Kifayah is based on the concept of poverty and not strictly based on Nisab. Nonetheless, the concept is same whereby the eligibility rests on deficit of funds for meeting basic needs.

Zakat eligibility is measured through Hadd-ul-Kifayah, which is a sort of poverty line, derived from measuring the value of basic needs.

Every state has their own Hadd-ul-Kifayah forms and details.

The selection of Asnaf depends on the calculation of Hadd-ul-Kifayah (sufficient limit) for each state. The Hadd-ul-Kifayah refers to six hierarchies which are:

- i. Shelter/accommodation
- ii. Medicine
- iii. Food
- iv. Education
- v. Clothing
- vi. Transportation

The eligibility check is performed each year. People have the perception that Zakat is like pension. Once qualified, they expect to receive Zakat every year. It may happen that certain people receive Zakat not just in one year, but in multiple years, but continuous payment is not required. In fact, it is not even allowed if a person reaches Hadd-ul-Kifayah and is no longer eligible to receive Zakat. Re-evaluation and screening is done each year to determine fresh standing of individual against the Hadd-ul-Kifayah criteria.

For instance, the Hadd-ul-Kifayah form in Kedah State has following key features:

- ❖ Identification of category of Asnaf (from the eight heads of Zakat).

- ❖ Identification information of the applicant including name, address, telephone number, bank account number, mosque, district, and identity card number.
- ❖ For checking eligibility, some additional information is also sought, such as marital status, pole number of electricity service, physical health status and smoking habit.
- ❖ Purpose of applying for Zakat funds.
- ❖ In asking for source of income, income of main applicant, spouse and children is also asked, including those living together as well as those living separately. Assistance sought from poor student trust fund, government assistance and other sources is also asked and confirmed.
- ❖ Details of expenditures are also taken into account, such as expense on food, clothing, education, medicines, transportation and other expenses.
- ❖ Details of residence are also asked including whether the house is owned or rented. Utilities used in the house including electricity, water and telephone are also probed. The condition and construction of the house is also asked and verified to get more information about the applicant's neediness.
- ❖ Information about vehicles is also asked, such as motorcycle, car, etc.
- ❖ Since Malaysia is a documented economy, the identity card can reveal many of the assets owned and contracts entered into by the applicant.
- ❖ Documents are verified through official documents, such as salary slips (for job income), house ownership documents (for house ownership), rental contract (for rental income/expense), bank statement (for bank balance), vehicle ownership document (for vehicle ownership), marriage certificate (for marital status), police report (for criminal record), photos of fire (for ascertaining emergency), pictures of residence (for ascertaining built structure and quality), birth certificate (children's identification), school fee voucher (for schooling and educational expenses) and so on.
- ❖ Verification is done by multiple signing authorities from Amil Assistant to the executive staff.

Similarly, Pusat Pungutan Zakat MAIWP also has a Hadd-ul-Kifayah form which asks for the following information and processes it to determine eligibility.

- ❖ Income of head of family, spouse and other income including income support from children, JKM assistance, house rentals, savings income, etc.
- ❖ Details of vehicles and house is also asked.
- ❖ Then, household expenditure is estimated by first asking about the household members and ages of school-going and non-school-going children.
- ❖ Health related issues in family including people with disabilities and chronic pain is also inquired in the form.
- ❖ Based on average expenditure budget allocated on each household member and for health related expenses, a normal average budget for the household is estimated.
- ❖ If the income of the household exceeds the household expenditure budget, then the applicant is considered non-eligible to receive Zakat.

- ❖ However, if the income of the household comes out to be lower than the household expenditure budget, then the applicant is considered eligible to receive Zakat.

Hadd-ul-Kifayah is used with a margin of discretion allowed. In marginal cases, other information is also used to decide whether to approve the case or not. Hadd-ul-Kifayah in value terms is different in different states. The reason is that the cost of the basket of goods is different across states and across rural and urban areas.

#### 5.1.6.2. Asnaf of Zakat

Asnaf of Zakat are beneficiaries. The list is based on Qur'anic verse 60 in Chapter Tawba. The list includes following beneficiaries:

- ❖ Poor with no assets and insufficient income.
- ❖ Poor with insufficient income.
- ❖ Workers working on administration of Zakat.
- ❖ New Muslim converts.
- ❖ People in bondage.
- ❖ People under debt.
- ❖ People working in way of Allah.
- ❖ People stranded as travelers.

The share of Amil shall not be more than one-eighth (12.5%) of total Zakat collection.

The administrative expenses for collection and distribution are borne from Zakat funds and 12.5% (1/8) value of Zakat funds collected are allocated for this purpose. If expenses exceed the ceiling percentage, then government supports the department. However, most of the time, the expenses are lower, and the surplus is allocated to various categories.

Spending in Amileen head can include salaries and administration expenses including utilities and overhead expenses. Pusat Pungutan Zakat MAIWP even tries not to use this much amount and reduces Amileen budget to one-sixteenth based on Fatwa. In the federal territory, the expenses are managed within the limit of 6.25%.

#### 5.1.7. Disbursement Schemes

There are various disbursement schemes offered by SIRC's in Malaysia. They range from cash transfers to funding schooling, hospitalization and providing business support. In educational schemes, scholarships are also offered along with uniform, fees, books and stationery. In health schemes, medical services, hospitalization, medicines and treatment is offered. Lembaga Zakat Negeri Kedah has an in-house dialysis facility for Zakat-eligible patients.

One good feature in the disbursement schemes is the synergy created in the ecosystem through productive Zakat and consumptive Zakat. Business tools, such as sewing machines are distributed among the deserving Mustahiq. They produce school uniforms, which are then provided to the schools. Likewise, rice is grown in paddy fields and distributed among the deserving families.

In the federal territories, there are 30 Zakat assistance schemes, conducted by Majlis Agama Islam Wilayah Persekutuan (MAIWP). They are outlined in Table 9.

**Table 9: Zakat Assistance Schemes in Federal Territories**

Category	Types of Aid
1. Welfare	1. Monthly Financial Statement 2. Aidilfitri Aid 3. Khairat Aid 4. Debt Settlement Assistance 5. Marriage Aid 6. Syarie Legal Assistance 7. Emergency help 8. Fare Assistance and Personal Needs 9. Disaster Aid
2. Medicine	10. Medicine Aid
3. Protection	11. Home Rent Deposit Aid 12. Home Renovation Aid 13. Home Purchase Deposit Aid
4. Da'wah and Wellness	14. Dakwah and Charity Activities Aid 15. Tahfiz Institute and Shelter House Aid
5. Economy	16. Business and Entrepreneurship Guidance 17. Agriculture/Fisheries/Agriculture Aid 18. Motorcycle Aid for People with Disabilities 19. Business Vehicle Deposit Aid 20. Taxi Rental Deposit Aid
6. Education	21. School On-Boarding Aid 22. Clothing and School Equipment Aid 23. Tuition Assistance Aid 24. IPT Preparation Aid 25. Special Incentive Scholarship 26. Al-Quran Memorization Incentive Aid 27. PICOMS International University College (PIUC) Tuition Aid 28. Baitulmal Professional College Kuala Lumpur (KPBKL) Tuition Aid 29. Industrial Skills Training Aid 30. Islamic Religion Aid

There is no strict ceiling defined for each scheme. Allocation depends on neediness and eligibility. Once eligibility criteria are met, it is not necessary that every family shall receive the similar amount of cash transfer. The amount of Zakat paid depends on the requirements and

eligibility. Zakat payment can range from RM 1,000 to RM 3,000 depending on the need and circumstances of Mustahiq. Non-Muslim converts are also supported from the Zakat funds.

Religious scholars in Malaysia interpret Tamleek as having wider meaning which can include physical ownership and possession and/or beneficial ownership. Hence, Kolej Universiti Antarabangsa MAIWP (UCMI) was established through Zakat funds. Zakat can be used to provide direct assistance to Asnaf or to provide beneficial services to them through building institutions.

In Indonesia and Malaysia, Fi Sibilillah includes:

- ❖ Dawah activities (individuals and organizations).
- ❖ Seminars, workshops and activities carried by universities, schools and associations that help to develop Muslims, especially students and youths.
- ❖ Publications of Dawah materials/books.
- ❖ Aid for disasters.

Zakat funds can be invested. For instance, buying shares from Zakat money for the children of Asnaf. This way poverty can be stopped from running in generations.

However, Zakat for Qard al-Hasan is not used in Malaysia. There is use of Zakat for providing Qard al-Hasan in Banda Aceh part of Indonesia and in Kuwait. But, due to the fact that Qard does not represent ownership and the funds return back to the lender, most Ulema globally and also in Malaysia do not allow it.

One justification for use of Zakat in Qard al-Hasan uses the logic that the loan is to be returned when the person has acquired profits. It means that the same loan amount is not returned back to the lender, but the profits are used for repayment.

However, whatever amount is used to return back the loan, it is still a payment by the Asnaf to the Muzakki or Muzakki's agent. Zakat receiver shall have complete ownership of the Zakat funds for Zakat to be considered paid. If he has to pay back the same amount later which was received as Zakat, then, it does not fulfill the condition of payment of Zakat according to majority of scholars.

Zakat is also used to provide assistance to foreigners. For instance, foreign students are helped from the Zakat funds. Once the funds are received, foreign students can remit their funds overseas as well. Under special circumstances, Zakat funds are also sent to deserving areas outside Malaysia. Cryptocurrency is also used to transfer payments to Palestine in a special arrangement.

Pusat Pungutan Zakat MAIWP also has a Muzakki Kafalah scheme. If the Zakat payer dies and has been donating Zakat of RM 50 per year or more, then the legal heirs will receive a lump sum amount, but that will not be Zakat money. It means that it is not necessary to check whether heirs are Sahib-e-Nisab or not.

### 5.1.7.1. Disbursement Method

In some states, collection and disbursement is done both by the Zakat department. For instance, in Kedah, both collection and disbursement function is performed by Lembaga Negeri Zakat Kedah. On the other hand, in the three federal territories, Pusat Pungutan Zakat MAIWP performs the collection function and Bait-ul-Mal performs the disbursement function.

When it comes to making payments to the Asnaf, Malaysia has high financial inclusion rates. 99% of the population living in sub-districts has access to financial services. 96% customers have active deposit accounts. Therefore, the banking channel is used for collection and disbursement. It ensures documentation which can be accessed, traced and easily documented. It significantly reduces chances of misutilization of funds.

## 5.2. Notable Points in Administration and Practice

### 5.2.1. Public-Private Partnership

Some states in Malaysia are active in engaging academia and industry. For instance, Kedah State collaborates with universities to conduct joint researches. It has approved and facilitated more than 200 research studies on Zakat.

Likewise, Zakat administration in the states offer assistance to businesses to calculate their Zakat. Kedah State acknowledges businesses which pay Zakat to the Lembaga Zakat Negeri Kedah by allowing them to use a logo on their product labelling. This way, Kedah State attempts to also tap corporate social responsibility-related spending.

Most states also have liaison with banks to allow auto-debit as well as periodic debit instructions. Banks also add a payment feature in their app so that online and mobile banking users can pay their Zakat online as well.

### 5.2.2. Use of Technology

Nowadays, Zakat institutions have implemented fintech technologies in the collection and distribution of Zakat. For example, in the federal territories, people can pay Zakat through online banking, portal, e-wallet and QR code.

States in Malaysia leverage the benefits of technology. For instance, Kedah State has launched Zakat on Touch app. It is a mobile application for the use of public users, charity assistants and Kedah Darul Aman Zakat Board staff. The app has been downloaded by more than 10,000 users on Google Play.

Various states in Malaysia have implemented fintech technologies for collection and disbursement of Zakat, for example, online banking, portal, e-wallet and QR code for Zakat payment in the federal territories, Zakat on Touch app by Kedah State, MyZakat app by Pusat Pungutan Zakat MAIWP, etc.



Likewise, Pusat Pungutan Zakat MAIWP has launched MyZakat app. It facilitates the user to fulfill Zakat obligation in a faster, easy and safe way anywhere and anytime. Users can calculate Zakat payment through the provided calculator. They can pay their Zakat through internet banking, Islamic credit card or debit card and check their previous Zakat payment record. The app has been downloaded by more than 10,000 users on Google Play.

Through in-house ERP system, most states showcase their live collection and disbursement figures on their website to ensure timely reporting and transparency. Trust is built between Muzakki (Zakat payer) and Mustahiq (Zakat receiver) through real-time reporting of both the collection amount as well as disbursement amount.

### 5.2.3. Reporting and Audit

#### 5.2.3.1. Reporting

Documentation of disbursement is also vital in order to build trust of people paying Zakat. Documentation through reports, real-time digital reporting and visuals is important. Pictures or videos tell the stories of change and motivate more people to contribute to the causes and schemes. Each state reports its activities through documented reports together with pictorial and visual summary of campaigns.

Annual reports are published which carry details of financial information along with information about events, campaigns and distribution ceremonies. Lembaga Zakat Negeri Kedah also publishes a list of top 10 payers and receivers, which encourages more philanthropists to come forward and have motivation to contribute.

Reporting of beneficiaries is also available publicly which ensures transparency. Dignity of individuals is ensured by only mentioning the name. In Kedah, CEO of Lembaga Zakat Negeri Kedah, Dato Sheikh Zakaria himself participates in disbursement activities by handing over food packs, cheques and equipment to the beneficiaries in ceremonies in a dignified and respectable way.

Furthermore, to convey correct information about the Zakat department at various forums, Lembaga Zakat Negeri Kedah has developed an internal research department. It produces research on topics of interest such as whether Zakat reaches needy and whether the process of shortlisting is efficient or not. In addition, this department makes liaison with universities for conducting research on various topics of mutual interest. They also fund such proposals up to some upper limit. The department provides data and other help for the conduct of research studies on Zakat. Zakat department disseminates such researches by using IT-based tools so that everyone can know about the activities of Zakat while sitting at home. All IT-based development has been made by indigenous human resources, which shows the presence of adequate human resource with them.

Lembaga Zakat Negeri Kedah also seeks regular feedback from more than 200 influential Ulama about the positive or negative aspects in operations of the Zakat department. The

department brings reforms in the light of their feedback. This provides them a sense of inclusiveness and enhances their trust in Zakat department. In addition, a link remains alive between Ulema and Zakat department.

#### 5.2.3.2. Audit

Both internal and external audits are conducted. The external audit is done by the Auditor General. Clause 35(1) of Enactment 23 of State of Kedah Dar ul Aman stipulates that ‘The board shall not later than April 30 every following year, submit the financial statements of the foregoing year, cause its accounts are to be audited by the Auditor General and shall as soon as practicable, submit the audited accounts to the state authority’. Sub-Clause 2 further adds that ‘The audited accounts shall be published in the Gazette’.

Scope of audit includes both physical audit as well as audit of documents and records. Reporting and audit are also subject to the administration of the State Islamic Religious Councils. For instance, audit of PPZ-MAIWP is mostly in the scope of financial audit by MAIWP. PPZ-MAIWP is also recognized in ISO QMS, ISMS and ABMS and is audited annually.

### 5.3. Challenges in Zakat Administration

There are some notable challenges in Zakat administration, which are outlined below:

- ❖ Zakat is not mandatory like tax. Hence, people do not give it as much importance as they would give to tax. Not paying Zakat is not a legal offence. A bill has been presented for legislation to make Zakat mandatory, but there has not been any development in this regard yet.
- ❖ In some regions, there is no Zakat act. No Zakat act at federal level is also a hindrance.
- ❖ Even though Zakat collection has been increasing, but in comparison to the need of funds, there is still a gap between collection and coverage. Not enough assistance could be provided to each and every family.
- ❖ Zakat funds need to be disbursed in short term. Sometimes, there are contingencies like Covid-19. In such times, more assistance is required. However, the current collection drops due to economic recession and because people start selling their Zakatable assets. Lapse of funds and not having enough funds in reserve during contingencies create challenges.
- ❖ The traditional view on Zakat still leaves out a lot of forms of wealth and income outside of Zakat and Ushr net. Not allowing Zakat in microfinance also limits the role of Zakat.
- ❖ Trust is the main challenge in Zakat management. The Zakat system must utilize technology effectively to track and get new payers for Zakat collection.

## 5.3.1. Points of Similarities Between Zakat System in Malaysia and Pakistan

**Table 10: Similarity in Zakat System of Pakistan and Malaysia**

Pakistan	Malaysia
Istehqaq determined based on neediness looking at income, assets, expenses and status of dependents.	Istehqaq determined based on neediness looking at income, assets, expenses and status of dependents.
Disbursement schemes are various and focus on cash transfers, health and education.	Disbursement schemes are various and focus on cash transfers, health and education.
Disbursement function is decentralized at the level of provinces and districts.	Disbursement function is decentralized at the level of states and districts.
Internal and external audit performed.	Internal and external audit performed.
Zakat law is in place in all provinces.	Exclusive Zakat law is in place in most states. In states where there is no Zakat law, other legislation and Fatwa Council guidelines govern the framework.
Funds lapse. Collection and disbursement almost equal with no reserve fund.	Funds lapse. Collection and disbursement almost equal with no reserve fund.

## 5.3.2. Points of Differences Between Zakat System in Malaysia and Pakistan

**Table 11: Differences in Zakat System of Pakistan and Malaysia**

Pakistan	Malaysia
Silver Nisab is used for determining Zakat obligation.	Gold Nisab is used for determining Zakat obligation.
Nisab for gold is 87.48 grams and for silver, it is 612.32 grams.	Nisab for gold is 85 grams and for silver, it is 595 grams. It is similar in Indonesia and Brunei as well.
Collection not done by provinces and districts. Collection only happening via banks, (deductions from PLS saving accounts in banks) and no collection mechanism in place for collection of Zakat from the general public.	Collection done by states. Very well developed systems in place for collection of Zakat from the general public. Major time and effort of the department is spent on collection of Zakat.
No collection by provinces. Only one-time transfer from federal to provinces.	Collection is done year-round. Disbursement also happens year-round.
Cash transfer amount is fixed. Either it is given or not given at all. No mechanism for adjusting benefits level benchmarking/indexation (according to inflation, wages, etc.) in place.	Cash transfer varies according to the neediness. Hadd-ul-Kifaya level determined on the basis of cost of basic needs and estimation of subsistence level essential households' expenditure.
No role of mosque and imam in Istehqaq determination or in disbursement.	Imam of mosque is engaged as Amil Assistant to perform role of collecting agent

Pakistan	Malaysia
	and also to verify eligibility. Mosques in Kedah have food banks.
Zakat can be used only for literal physical transfer of ownership of Zakat amount (i.e. the condition of Tamleek).	Zakat can be used for beneficial ownership. Hence, funds can be used for development of service infrastructure that will help the Asnaf. For example, UCMI University was built with Zakat funds as well as Asnaf School in Kedah. Hemodialysis center was built in Kedah from Zakat funds.
No Zakat calculators on website and app.	Zakat calculators are available on website and app.
No assistance for Zakat assessment available at head office and district office since collection is not decentralized currently.	Zakat assistance for assessment is provided via mobile counters, hotline, meeting appointments and consultation to walk-in visitors.
No collection mechanism of Zakat from public exists. Almost all collection is deducted at source on financial assets/income.	Active collection drive through bank, monthly payment plans, standing instructions given to bank, mobile wallet, walk-in donations, mobile vans, and 'drive to you' facility which collects Zakat on the spot.
No tax rebate. Only tax relief is that payment of Zakat can be used for reducing taxable income.	100% tax rebate to individuals and 2.5% tax rebate to businesses on their aggregate annual income.
Formal annual reports are not published. Only summary statistics are available. No visual documentation of events or newsletters.	Corporate video exists. Visual documentation of events. Formal annual reports are published. Real time reporting of collection and disbursement.
Only group secretaries and auditors are paid from Zakat funds to the extent of 10% of Zakat funds.	12.5% (1/8) value of Zakat funds can be used for Zakat administration. Expenses are not limited to payment of salaries, but other necessary expenses to carry out effective Zakat collection and disbursement.
No linkage and synergy and graduation measures between programs.	Graduation measures for productive inclusion in programs. For example, productive Zakat recipients receive sewing machine to produce uniforms that are provided to the children of Asnaf. Rice produced in paddy fields is distributed among Asnaf.
No productive Zakat. Only skills-based education provision is there from Zakat funds, which, too, has been suspended in KP.	Zakat is used in both consumptive and productive purposes.

Pakistan	Malaysia
Livestock Zakat, Ushr, Zakat on gold, etc. not received. Also no Zakat-ul-Fitra and Fidyah.	Livestock Zakat, Ushr and Zakat on gold is received. Also Zakat-ul-Fitra and Fidyah.
No business Zakat is received.	Business Zakat is received. Businesses are provided permission to use logo of Muzakki.
Zakat is not used for investment purposes on behalf of Asnaf.	Zakat is also used to buy shares in enterprises for children of Asnaf.
No in-house Mufti or Shari'ah advisor.	Fatwas of Religious Council guide the operations of Zakat administration.
Zakat is used mostly in providing cash transfers to the poor.	Zakat is used in all various heads of Zakat. Kedah State has a Muallaf center as well for new Muslim converts.
No Wakalah scheme for encouraging people to pay through Zakat Department or engage NGOs as Wakeel.	Pusat Pungutan Zakat MAIWP has Wakalah scheme whereby people can pay Zakat to them. Then, they have the right to pay up to 50% of the funds to the identified beneficiaries.
No Zakat training or academy.	Kedah has International Zakat Academy providing training for Zakat administration to global players as well. Pusat Pungutan Zakat MAIWP also has Zakat academy for publishing books, reports and journals.
No role of mosques and imam in assessment and collection formally.	In State of Kedah, imam plays a pivotal role in identification of Mustahiq and verifying Hadd-e-Kifayah.

#### 5.4. Overview of Waqf in Malaysia

Waqf refers to permanent dedication by a Muslim of some movable and immovable assets in the cause of Allah so that its benefits can accrue to the beneficiaries. The purpose shall be recognized by Shari'ah. For instance, it could be religious purpose or charitable purpose.

If the beneficiaries or beneficial use is specific, then it is known as Waqf Khas (Waqf Specific). For instance, the Waqf of land for Masjid falls under Waqf Khas. Waqf Khas is a dedication in perpetuity of the capital of property for pious, religious or charitable purposes recognized by the Muslim law. The income of the property is paid to persons or for purposes specified in the Waqf and the property so dedicated.

Waqf Aam (Waqf General) has no restriction on beneficial use and beneficiaries and is more flexible. Waqf Aam means a dedication in perpetuity of the capital and income of property for pious, religious or charitable purposes recognized by the Muslim law.

In Malaysia, Waqf administration falls under the jurisdiction of State Islamic Religious Council in each state and federal territories. The objective of Waqf administration and management is

to develop and manage Waqf property whether it is movable or immovable property and responsibilities include maintenance, investment, construction, and providing services.

Mobilizing resources is also part of the core functions. Making effective use of Waqf property and assets through planning, development, joint ventures and investments is part of the responsibilities.

There are various types of Waqf common in Malaysia including:

- ❖ Waqf for Housing
- ❖ Waqf for Health
- ❖ Waqf for University
- ❖ Waqf Al-Qur'an
- ❖ Waqf for Religious Books and Dawah
- ❖ Waqf for Education
- ❖ Waqf for Agriculture
- ❖ Water Supply Waqf

Auqaf hotels are the recent trend in the development of Waqf property. Four hotels have been built under the Waqf concept in the states of Malacca (Pantai Puteri), Perak (The Regency Seri Warisan), Terengganu (Grand Puteri) and Negeri Sembilan (Klana Beach Resort).

Some statistics related to Waqf land in Malaysia are given in Table 12.

**Table 12: Waqf Land in Malaysia**

Key Indicators	Figures
Total Land Size in Hectares	30,889
Total Land Size in Acres	76,328
Total Number of Lots	14,536
Percentage of Land Developed	11%
Developed Land Area in Hectares	3,505
Undeveloped Land Area in Hectares	1,237
Land Area with No Development Records	26,147
Percentage of Land with No Development Records	85%

Table 13 summarizes the Waqf land state-wise. Most Waqf land concentration is in the State of Perak. It is followed by Johor and Sabah. All the other states combined have only 10% of remaining Waqf land.

**Table 13: Waqf Land in States**

State	Land Area (Hectares)	Percentage
Perak	20,225.75	65.5
Johor	5,149.10	16.7
Sabah	2,130.04	6.9
Kedah	820.31	2.7
Pulau Pinang	742.01	2.4
Terengganu	484.10	1.6
Melaka	357.04	1.2
Selangor	352.67	1.1
Kelantan	284.92	0.9
Sarawak	143.68	0.5
Perlis	83.22	0.3
Pahang	74.60	0.2
W. Persekutuan	24.27	0.1
Negeri Sembilan	17.18	0.1

#### 5.4.1. Legal Framework of Waqf in Malaysia

Waqf affairs are the responsibility of the Islamic Religious Council of each state. Section 25 of the Civil Law Act, 1956 states that the administration of Muslims' property shall be in accordance with the Islamic law. Jurisdiction over Waqf lies within the purview of the Syariah Court List II (1) of the Ninth Schedule of the Federal Constitution.

Each state has its own legal framework. For instance, Johor Wakaf Rules, 1983, Enactment of Wakaf (State of Malacca), 2005, Enactment of Wakaf (Negeri Sembilan), 2005, Waqf Enactment (Selangor State), 2015, Waqf Enactment (State of Perak), 2015, Waqf Enactment (State of Terengganu), 2016 and Sabah State Waqf Enactment, 2018 are some of the Waqf laws in the states.

In the states where there is no specific law, Islamic law has certain relevant sections on Waqf. For instance:

- ❖ Penang: Islamic Religious Administration Enactment (Penang) No. 4 of 2004 (Sections 89-95).
- ❖ Perlis: Islamic Religious Administration Enactment (Perlis) No. 4 of 2004 (Sections 89-95).

- ❖ Pahang: Islamic Law Administration Enactment (Pahang) No. 3 of 1991 (Sections 67-81).
- ❖ Kedah: Islamic Law Administration Enactment (Kedah) No. 5 of 2008 (Sections 52-58).
- ❖ Kelantan: Enactment of the Council of Islamic Religion and Malay Customs (Kelantan) No. 4 of 1994 (Sections 61-66).
- ❖ Sarawak: Sarawak Islamic Council Ordinance 41 of 2001 [Part V – Establishment of Baitulmal and Waqf Board, Baitulmal, Waqf and Nazir (Sections 43-55)].
- ❖ Federal Territory: Islamic Law Administration Act (Federal Territories) Act 505 of 1993. Part VI – Finances (Charitable Trusts) (Sections 60-71).

These enactments stipulate that State Islamic Religious Council shall be the sole trustee of all Waqf. One of the important characteristics of Waqf in Malaysia is that every Waqf shall be registered in the name of the Islamic Religious Council as proprietor in accordance with the National Land Code, 1965.

Since Ahadith mention that one cannot leave a will to dedicate more than one-third of wealth to other persons apart from legal heirs, Waqf of more than one-third of wealth is considered invalid. State of Pahang, Malacca, Pulau Pinang, Kedah and Perlis have the same application except Kelantan and Terengganu where the ruler can validate it.

When someone wants to create a Waqf, he is required to transfer the land to the Majlis. The Majlis then becomes the administrator of all Waqf property. Every Waqf then shall be registered in the name of the Majlis as proprietor in accordance with the National Land Code, 1965. All of the Mawquf and Waqf property must be declared in the gazette under the administration of the Majlis.

The Department of Wakaf, Zakat and Hajj (JAWHAR) was established in 2004 under the Prime Minister's Department to oversee the management of Waqf resources in the country. JAWHAR has published manuals for land Waqf management, Istibdal in Waqf and Cash Waqf.

#### 5.4.1.1. Allowance of Istibdal of Waqf in Malaysia

Istibdal as a substitution of Waqf property with another property or cash either through substitution, purchase, sale or any other way that is approved by Syariah principles. Substitution can be divided into two forms, i.e.

- ❖ Substitution of one Waqf with a similar one.
- ❖ Substitution of land with its cash value.

The National Fatwa Committee on April 22, 1999, issued a Fatwa that the practice of Istibdal is permissible provided that the acquired or transferred Waqf land by the government shall be compensated with the same value or be substituted with another land.



The 80th Muzakarah of the Fatwa Committee of the National Council for Islamic Religious Affairs Malaysia held on February 1-3, 2008, discussed the law for developing special Waqf land with development other than the original intention of the Waqf.

The Muzakarah agreed to decide that developing special Waqf land, especially mosque Waqf with additional development projects, or improvements to ensure that the Waqf property remains intact is allowed by Islam provided this development must be based on needs that can be determined by the government and are not in conflict with Shari'ah.

The concept of Istibdal is utilized in several forms such as:

- ❖ Selling part of the Waqf property to develop the remaining part of the same property,
- ❖ Selling bundle of Waqf properties and buying new one in exchange to be used for the same purposes of the sold properties,
- ❖ Selling one Waqf and buying another having common purpose and
- ❖ Selling a handful of properties belonging to various Waqf and buying a new property which has higher income.

The Majlis may substitute any Waqf property, when it is no longer beneficial as intended by the dedicator and in the event that the usage of Waqf property does not meet the actual purpose of Waqf.

#### 5.4.1.2. Legal Status of Cash Waqf in Malaysia

Legal framework in Malaysia allows Cash Waqf. Reasoning used is that Waqf asset or capital has to remain in perpetual existence. But, returns earned from investments can be used to provide beneficial services through Cash Waqf. Thus, capital in Cash Waqf is invested in safe investment options and the return earned on investments is used to provide different beneficial services.

Cash and Corporate Waqf are legally acceptable and acknowledged in Malaysia, which helps in diversity of donations.

Allowance of Cash Waqf enables divisibility of donations. Not many people can donate real estate. However, they can contribute their pro-social savings in the form of cash. The cash resources pooled through many people can still enable the provision of required infrastructure and services for the beneficiaries.

License of crowdfunding is required from the securities commission. Therefore, it is not legal to mobilize cash from people without having the necessary license and approval from securities commission of Malaysia.

#### 5.4.1.3. Legal Status of Corporate Waqf in Malaysia

Corporate Waqf is defined as a type of Waqf where the Mawquf (Waqf assets) are in the form of shares issued and managed by a corporate entity. Malaysia also allows corporate sector

involvement in Waqf. Johor Corporation was a pioneer example of Corporate Waqf in Malaysia. It is engaged in agribusiness, real estate, food business and health sector. Waqf An-Nur is another organization which looks after management of mosques and clinics.

The corporation must be established under the Companies Act, 1965 as a company limited by guarantee. The Corporate Waqf must have been appointed as a Nazir or Mutawalli by State Islamic Religious Council.

Usually, 70% of the profits are reinvested in business and up to 30% of the profits are used for charitable purposes. This way, social services are also provided in the corporate setup which tries to run the enterprise in a profitable way so that the scale of beneficial services can be extended.

#### 5.4.2. Integration of Waqf with Zakat in Malaysia

Zakat and Waqf are used together as well in providing beneficial services through institutions like health institutions and educational institutions. Waqf can be used to provide infrastructure and real estate for the establishment of institutions. On the other hand, Zakat can be used to provide income support and free services to the Asnaf through those institutions.

Co-financing of projects this way helps in covering both fixed and variable costs and increases the pool of funds available for the provision of beneficial services.

#### 5.4.3. Public-Private Partnership in Waqf Development in Malaysia

Waqf resources in the form of immovable assets like property and movable assets like cash are managed in a way to achieve growth as well as ensuring preservation. Land is developed through joint ventures with builders.

Project financing is either facilitated through internal funds or through engaging financial institutions like banks.

In the joint venture model where profit sharing is involved, a developer is engaged to develop the property. Waqf department provides land for development. Developer develops the land for onward lease to the clients. Rental revenues generated are shared on profit-sharing basis.

Project development is done either through self-development or by engaging developer as a project management consultant. Joint venture (JV), build, operate, transfer (BOT), and design and build models are also used. Sometimes, government grants are also used for funding.

For example, in Penang, Majlis Agama Islam Negeri Pulau Pinang (MAINPP) will provide the land as a project site. The developers will develop the land using their own capital. The project land site cannot be pledged to any financial institution for the purpose of obtaining a bridging loan. MAINPP can only lease the Waqf land to buyers/tenants. Lease period is subject to MAINPP approval.

The buyer can obtain end financing from any financial institution through Ijarah according to the decision of the Penang Fatwa Committee No. 2/2006 dated November 30, 2006.

It must be noted that only Muslims are offered to buy this property. The lease transfer is from Muslims to Muslims only. All financial systems should only use Islamic banking.

MAINPP's developed lands are in accordance with the technical requirements of the local authority. However, the land involved with the road, open space, sewage plant, TNB sub-station is not transferred to the state authority.

The design of residential houses should be in accordance with the way of Muslims' life. If there are no physical and cost obstacles, the bathroom/toilet should not be built facing the Qibla. In MAINPP lands, it is not allowed to build objects that are against the Islamic religion such as temples, idol houses and so on.

#### 5.4.4. Housing Ownership through Waqf

UDA Holdings is engaged by the Council to construct buildings over Waqf land. It builds low-cost apartments with an aim to provide affordable housing to Muslims in Malaysia. Usually, 30% of the units are reserved for Bhumiputra.

Ijarah financing is also involved to facilitate house ownership. Banks are sometimes reluctant and raise their risk premium in quoting rental rate in such projects since they know that ownership cannot be transferred and ultimate ownership rests with State Islamic Religious Council.

Land remains the property of State Islamic Religious Council. Land cannot be sold, charged and surrendered. Sales execution is done via Form 15A (Lease). The Council may lease the developed unit for 99 years and the land will return to the Council after the lease term is over. Extension of lease can be done after the lease term is over.

Some banks provide financing, such as Bank Muamalat, Bank Islam and Bank Nasional. State Islamic Religious Council may lease the developed unit to a bank for 99 years. The bank may lease the developed unit for 25 years. For the remaining lease period (99 – 25 years), the bank may lease the unit to subsequent lessee/fourth party.

In joint venture business model, State Islamic Religious Council would act as a land owner to provide Waqf land. UDA would act as a developer to develop the Waqf land. UDA will bid to get the land for development. The bid price could be at a 20% premium to the current value of land. Cost will be covered through development and subsequent lease. In case, the property overlaps with some public infrastructure, such as public amenities, power supply station, green area, pond, drainage, sewerage treatment plant and road, such shall be surrendered to local authorities. However, Shari'ah principles stipulate that Waqf land cannot be surrendered to any other authority after its permanent and perpetual dedication to Allah.

Such development has other socio-economic benefits. For instance, it creates business in sub-sectors that are connected to the construction sector.

More jobs are created for masons, plumbers, electricians, technicians and heavy equipment operators. Businesses get more revenues by supplying building material, such as cement, limestone, bricks, paints, construction tools, construction equipment, construction gear, roofing, sanitary, furniture and consumer appliances. Machinery manufacturers and operators also get business and jobs with increased demand for excavator, bulldozer, tractor, lorry and backhoe.

Skillful workers also get greater job opportunities, such as architects, mechanical engineers, electrical engineers, land surveyors, real estate analysts and so on.

Economic activities are created through financial activities involving banks and advertising activities through advertising agencies and media. The government gets to collect more taxes and non-tax revenue from the documentation and registration. Utility companies get new subscribers and customers for water, electricity, telecom, internet, and fuel.

Through development, beneficiaries get direct benefit via low-cost housing, offices and shopping complexes. State Islamic Religious Council is able to enhance the value of Waqf property as well as its rent. More rental income and revenues enhance the capacity of carrying out welfare activities.

#### 5.4.5. Challenges in Waqf Management in Malaysia

Even though Malaysia is a very well documented economy, still there are some challenges in Waqf management. Some of these challenges are outlined below: -

- ❖ No land records in some areas since land has been existing long before independence. For unoccupied land in suburbs or in rural areas, development record is missing.
- ❖ Since ultimate ownership is not transferred on Waqf-based property, apartments and assets, banks are sometimes reluctant to provide financing.
- ❖ There is no tax exemption on Waqf at the moment. Same charges are levied on sale, exchange and income. Hence, lack of tax incentives sometimes dampen the use of Waqf.
- ❖ Local authorities want the surrender of area where some public amenities exist or planned to be developed, such as power supply station, green area, pond, drainage, sewerage treatment plant and roads. However, looking at it another way, a property or land area which had been dedicated in the way of Allah shall not be surrendered after its permanent dedication in order to ensure perpetuity and irrevocability.
- ❖ Majlis also faces a problem to develop Waqf land classified as heritage. This type of land is put under the auspices of the local authority and museum department.

- ❖ A lot of Waqf lands are located in scattered rural areas where potential for development and rise in value is relatively lower and due to scattered nature of lands geographically, there are limited economies of scale in development.
- ❖ A lot of people still do not have complete awareness of Waqf, its potential and impact.

#### 5.4.6. Similarities between Pakistan and Malaysia in Waqf Governance

**Table 14: Similarities in Waqf Governance in Pakistan and Malaysia**

Pakistan	Malaysia
Waqf law exists in provinces.	Waqf law exists in states.
Waqf is irrevocable after permanent dedication.	Waqf is irrevocable after permanent dedication.
Ultimate Nazir or custodian is Chief Waqf Administrator.	Ultimate custodian is State Islamic Religious Council.
One major source of revenue is rental income.	One major source of revenue is rental income.
Property Waqf has more significant share in Waqf economy.	Property Waqf has more significant share in Waqf economy.
Some examples of Corporate Waqf, e.g. Hamdard Laboratories.	Some example of Corporate Waqf, e.g. Johor Corporation, Waqf-An-Nur and Auqaf Holdings.

#### 5.4.7. Differences between Pakistan and Malaysia in Waqf Governance

**Table 15: Differences in Waqf Governance in Pakistan and Malaysia**

Pakistan	Malaysia
Cash Waqf is not allowed in legal framework yet.	Cash Waqf is allowed since 2007 as per 77th Fatwa Committee Muzakarah.
Istibdal (exchange) is allowed in extreme situations.	Istibdal (exchange) is allowed in extreme as well as beneficial situations.
No significant public-private partnership.	Public-private partnership, e.g. UDA Holdings develops Waqf land by construction work.
No new private Waqf created. Department is managing existing Waqf land only.	Establishing new private Waqf is common.
Waqf is not used usually for establishing welfare institutions.	Waqf is used for establishing welfare institutions, such as hospitals and educational institutions.
Trust model more popular than Waqf due to restrictions in governance, investment and exchange.	Waqf model is equally popular, especially among Muslims.

Pakistan	Malaysia
Waqf is confined to properties, such as mosques, religious schools and shrines. Some houses, shops, agricultural land and few petrol pumps, dispensaries and a marriage hall also exist.	Waqf includes both Property Waqf as well as Cash Waqf.
Income confined to rent and financial income on bank investments.	Income sources are various including rent, profit on sale, financial income and fees.
No private Mutawalli.	Private Nazir is possible for management, e.g. Mutawalli Corporate and Mutawalli Academic.
Limited cash mobilization on shrines. But no active formal banking and digital mediums are used.	Cash mobilization is carried out with option to contribute via multiple channels, including donation boxes, bank branch, online banking, mobile wallet account, QR code, etc.
No urge to commercialize Waqf properties for enhancing rental income.	Waqf property is developed and commercialized to fetch better rents as well as ensure effective use through building infrastructure for housing, hoteling, recreational activities and shopping centers.
Short-term lease renewable on Waqf assets is common with no development and under more depreciated state.	Waqf land leased to builders on long-term basis in joint venture to develop Waqf land.
Department's main role is to protect Waqf properties from deterioration, illegal occupation and encroachments.	Waqf is used for providing various economic services, such as housing, equipment, medical, rehabilitation and educational services.
Waqf properties are geographically dispersed which increases cost of maintenance, monitoring and reduces economies of scale in development and in fetching rents.	Waqf land is developed into apartments, and sale and lease of apartments fetches greater rent and value per area after development.

## Chapter 6

# Policy Recommendations for Using Islamic Social Finance Effectively for Extending Social Protection

This chapter provides recommendations after documenting the issues identified in primary data collection from the field in Chapter 4. Implementation of these recommendations and their effectiveness hinges upon political will and provided the government is able to win back the trust of people. Unless people have trust in the system, it is hard to engage them in a government-run program when a lot of other better managed institutions are filling the gap in private sector.

However, it is important to carry out reforms as currently the government-run Zakat system is seeing decline of funds and significance and has been confined to deduction of Zakat at source from bank accounts only.

Given the high state of poverty, deprivation and need for social protection among masses, the system needs to be revitalized to leverage the full potential of Zakat. The government has the human resources at the grassroots level to perform identification of beneficiaries. With reforms and recommendations suggested in this chapter, improvements can be brought in the administration provided the obstacles of political will and trust deficit are resolved.

Besides recommendations in Zakat and Ushr, this chapter also outlines recommendations in the governance and administration of Waqf in order to make effective use of Waqf properties and assets and utilize them for social protection.

### 6.1. Policy Recommendations in Zakat Management

#### 6.1.1. Recommendations in Assessment and Collection

##### 6.1.1.1. Enhancing the Coverage of Zakatable Assets

Islamic principles require that every asset that is purchased and held for the purpose of trade shall be subject to Zakat. Furthermore, all savings whether held in local currency, foreign currency, negotiable instruments, financial investments and bank accounts, shall be subject to Zakat on wealth as well.

In the light of this, it is recommended to extend the list of items in the First and Second Schedule of KP Zakat and Ushr Act, 2011 to cover contemporary financial, intangible and digital assets.

Contemporary financial assets shall now also include Sukuk. Likewise, intangible assets which are held for trade shall also be subject to Zakat. Finally, digital assets like wallet money in mobile account with bank or any payment platform is also Zakatable. It is important to mention these Zakatable assets in the Schedule of Zakatable assets in the KP Zakat and Ushr Act, 2011.

#### 6.1.1.2. Enhancing Coverage of Assets in Centralized Collection

Article 31(2c) of the Constitution of Pakistan 1973 urges the government to secure the proper organization of Zakat, Ushr, Auqaf and mosques. Therefore, in order to carry out this responsibility, the government should bring more items from the Second Schedule to the First Schedule in KP Zakat and Ushr Act, 2011.

For instance, current account and foreign currency account of individual persons. It is recommended to extend the list to include savings kept in other documented forms, instruments and platforms, such as Sukuk, mobile wallet accounts, etc.

Furthermore, it is also important to remove exemption to assets in the First Schedule, which are acquired in foreign currency, from compulsory Zakat payment in Section 3 of the Zakat and Ushr Act, 2011.

#### 6.1.1.3. Creating Awareness about Zakat for Enhanced Collection

It is important to create awareness among the masses for voluntary Zakat contribution. In the job description of group secretaries and auditors, conducting awareness seminars should be introduced. Since major disbursement of Zakat funds is in Guzara allowance at only particular times of the year, there is ample time with the staff to schedule these activities.

In order for the staff to provide awareness to the masses, it is important to give them training as well. Awareness seminars can be held in mosques, universities, colleges, schools and government departments. Upon request, such seminars can be arranged in offices, community halls and other community hotspots.

Similarly, members of the Local Zakat Committees should be motivated for sensitizing people in their respective areas about the importance of paying Zakat and guiding and counselling the communities in this regard. A mechanism for incentivizing could also be developed for encouraging them to do so. With such an extensive field formation of volunteers at grassroots level at the department's disposal, it can achieve great success in this area.

To sensitize people towards Zakat, Local Zakat Committees should provide guidance and counselling to their local communities, seminars should be conducted in educational institutions and government departments.



Use of digital and electronic media, especially social media platforms with smart communication material/messages, should be utilized for raising awareness among the general public in this regard. A communication strategy should be developed with the aim and objective of how best to reach out to the public, business communities, people in corporate/private and government service and those in various professions like doctors, engineers, lawyers, teachers, etc. using various modern and conventional tools and techniques.

For awareness, the website must be redesigned as well to add these features:

- ❖ User-friendly non-technical summary of major rules regarding Zakat. Animation, flowcharts and simple calculations can be used to explain the details.
- ❖ Frequently asked questions about Zakat should be posted. Smart search filters should show the relevant set of questions in search results. For this purpose, the documented Fatawa of Dar-ul-Ifta can be used as well. For instance, Jamia Binnoria Karachi has the largest online database of authentic Fatawa including Fatawa on Zakat. The valuable material can be used with permission.
- ❖ Zakat calculators need to be available visibly on the website. Zakat calculator should cover Zakat-ul-Maal, Zakat-ul-Ard and Zakat-ul-Ana'am.
- ❖ Consult a Mufti for features needed to be introduced on the website.

Mosques run under the Ministry of Religious Affairs or Auqaf Department should be utilized for creating awareness by making it mandatory to have one Khutba on Zakat once every quarter.

Liaison with proselytizing organizations like Tableeghi Jamaat, Dawat-e-Islami and others like Al-Khidmat Foundation can be explored to create awareness and sensitivity about Zakat. These organizations perform the task of preaching and reminding about Salat. They can be requested to also include Zakat in their agenda so that more awareness and sense of duty is created among the masses regarding Zakat. The Qur'an mentions Salat and Zakat together at multiple places and they constitute the second and third pillar of Islam, respectively. Hence, both are highly important in Islam.

#### 6.1.1.4. Facilitating Seamless Zakat Assessment

It is important to facilitate self-assessment through approved and interactive smart Zakat calculator on the website and Mustahiq app. The calculators shall help in calculating Zakat-ul-Maal, Zakat-ul-Ana'am and Ushr. The calculators should be smart enough to filter inputs to allow personalization, efficiency and user-friendliness.

In this regard, a telephone and internet hotline could also be introduced to answer Zakat assessment queries by scholars. A panel of scholars can be arranged for this to respond to the public's queries. This can be allowed on a limited scale first and it can eventually be scaled up. For instance, a few hours' slot every day of the week or on certain days.

To manage time and human resources, call center recording facility can be provided to the callers. They can record their queries and will be issued a ticket. The scholars engaged by the Zakat Department will answer these queries in sequential order.

On a pilot basis, WhatsApp chatbot service can be introduced for common questions. Banks and service sector institutions have already done this on their website as well as on WhatsApp. It will allow interactive communication and solve minor routine queries without the need to wait.

For those unable to access internet and the app, self-assessment forms must be developed in multiple languages with filtered criteria. Such forms should be made available at:

- ❖ Bank Branches
- ❖ Post Offices
- ❖ Designated Dar-ul-Ifta

People can be given the option to scan the forms and send to the WhatsApp number. The scholar at the Zakat Department can call back to confirm details and verify the amount of Zakat to be paid by the questioner.

#### 6.1.1.5. Crowdfunding to Match Funding Gap in Specific Causes

Introducing e-Crowdfunding platform on the website and mobile app can help in meeting the funding gap in specific causes and projects. It is important to allow ease in payment and work on impulse reaction when emotions and sentiments are triggered.

Interviews of beneficiaries, ceremonies, visual reporting and video snippets can document the work done under projects and it can help in creating awareness as well as building confidence and trust in the system.

One of the biggest problems in Zakat administration is lack of funds. If the funds are too little, then many well-meaning programs would not see the light of day. Hence, Crowdfunding is important to fund the disbursement needs if Zakat budget received from the federal government is exhausted and there are still deserving and verified beneficiaries who are looking to be catered.

Overseas Pakistanis can be attracted towards these open campaigns through push notifications to Roshan Digital account holders. This requires liaison with banks to allow a nicely placed tab on the website and app along with occasional pop-up notifications to elicit response towards contribution.

To increase Zakat collection, overseas Pakistanis can be attracted towards open campaigns through push notifications to Roshan Digital account holders.

#### 6.1.1.6. Introducing Incentives and Differential Treatment for Enhancing Zakat Base

Right now, income tax laws allow deducting Zakat as an expense to reduce taxable income rather than adjusting the tax liability itself. But, it would be a significant incentive to allow adjustment of tax assessed against payment of Zakat.

Hence, providing adjustment in assessed income to those who had paid Zakat can reduce tax evasion and encourage Zakat payment to the government for effective and targeted disbursement.

This is the practice followed in Malaysia and that is why, they have the largest central Zakat collection among all Muslim majority countries. Tax rebate on Zakat payment is available to the extent of 100%, but only if Zakat is paid to the government. In Pakistan, there is no such incentive yet.

Introducing incentives and differential treatment based on Zakat filer or non-filer is also an option that can be tried. It has successfully been applied by Federal Board of Revenue. For instance, a different tax on services income for Zakat filer or non-filer, a different rate of tax on capital gain depending on whether the person is Zakat filer or non-filer etc. Likewise, there can be differential treatment introduced in documentary duties as well on asset and property purchase and transfer, etc.

Introducing incentives and differential treatment based on Zakat filer or non-filer can be tried as successfully applied by FBR. Under this, there can be different tax rates for Zakat filers and non-filers.

#### 6.1.1.7. Establishing a Mechanism for Collection of Zakat from the General Public

Not only ATMs can be used to disburse payments to deserving beneficiaries, but they could be utilized for mobilizing charitable giving. Likewise, banks which provide discounts and reward points should engage with institutions providing welfare services to offer redeeming of points for provision of social services. Faysal Islamic Bank has already started that in Pakistan.

Careem also offers redemption of points for providing school books, meals, patient services and planting trees. Likewise, Facebook offered matching incentive on 'Giving Tuesday' for fundraisers. Such initiatives can enhance the effectiveness of mobilizing social crowdfunding.

The collection points and mediums can be enhanced by leveraging technology and allowing payment of Zakat on multiple payment gateways, including easypaisa, JazzCash, UPaisa, mobile banking apps and other frequently used apps such as for food delivery and ride hailing.

Due to high financial exclusion, physical cash collection is also an important medium in the current period of time. Mobile booths and counters should be set up at airports, railway junctions, universities, shopping malls, bank branches, post offices, etc. Collection receipt should be given with instructions to scan and send it to a WhatsApp number for counter verification.

Fund raising campaigns can also be organized in mosques, business centers, shopping complexes, universities and other community hotspots from time to time in order to raise awareness, provide real-time Zakat assessment, strengthen bonding and linkage with community and raise Zakat and donations.

#### 6.1.1.8. Enhancing Engagement and Utility of Mustahiq App

Checking eligibility is an important task in effective targeting, especially when the funds are constrained. It will be better to have all Istehqaq forms available in Urdu and regional languages, such as Pashto. In the Istehqaq form for Guzara allowance, following changes are suggested:

- ❖ While asking about source of assistance received from elsewhere, it is better to also ask how much assistance is received monthly or yearly.
- ❖ While asking for modes of transport, it is better to first ask whether any of these are in ownership, for instance motorcar, motorcycle, bicycle or animal cart. If no mode of transport is in ownership, then ask ‘how one commutes’. In this sub-question, options such as these can be given: bus, van, motorcycle rickshaw, taxi, online bike ride, online rickshaw ride or online car ride.
- ❖ Rather than asking for the number of shops, better to ask value of stock-in-trade, monthly turnover and trade debts to get an idea of scale and health of business.
- ❖ In asking for animal transport, also give option of horses, mules and camels.

### 6.1.2. Recommendations in Zakat Administration

#### 6.1.2.1. Removing Barriers for Community Engagement

The local Zakat committees work voluntarily. Such community engagement at grassroots level is vital in effective targeting. It is also cost effective since they work as volunteers. Pakistan is still a country with high school drop-out rate and low literacy rate, especially among the female population.

Hence, educational and age barriers should be removed that are not directly constraining the potential of work which can be provided by experienced, but non-matriculate males and socially active, but young and non-matriculate females.

Hence, matriculation requirement for members of local Zakat committee must be relaxed in view of general low level of literacy in some districts. Likewise, age restriction should be reduced for females. Nonetheless, there is a concern about comfort level of young females to get involved in local Zakat committee which is dominated by male members. Hence, this requirement should not be completely relaxed. But, it should be brought down from 45 years of age as stated in Section 12[c] of Zakat and Ushr Act, 2011.

On the other hand, it is better to also have minimum age requirement for male members. Girls and women also come in contact with local Zakat committee and often in dire circumstances of need. Married men at mature age would be better suited for the role of chairmanship and vice chairmanship in local Zakat committee.

#### 6.1.2.2. Creating Data Synergy for Effective Filtering

Zakat Management Information System is an excellent initiative by the Zakat Department to digitize records and help in informed decision-making and analysis. Each year, the data of new beneficiaries as well as applicants get documented. It is a very useful database to analyze impact assessments for past beneficiaries.

Creating synergy between databases is important to reduce duplication of cost and efforts, i.e. reinventing the wheel. It is important to leverage the efforts and resources already engaged in to collect data. It is vital to link the data of Zakat Management Information System (ZMIS) with Benazir Income Support Program to avoid:

- ❖ Double-dipping. For instance, one person taking assistance from both schemes at the same time.
- ❖ Double allocation to same beneficiary.
- ❖ Missing allocation to deserving beneficiaries. Exclusion Error.
- ❖ To counter verify and update information to create information synergies.
- ❖ Inclusion Error.

#### 6.1.2.3. Reducing Political Interference

It is important that the whole process from identification of the beneficiary to disbursement remains free of political influences and intervention. Reducing political interference in selection of DZC/LZC members is critically important as it jeopardizes the integrity of the whole system. In addition to that, using Proxy Means Testing based targeting can bring more transparency and objectivity in identifying targets. It is pleasing to note that the KP Zakat and Ushr Department is already using such a scorecard-based system.

Diversity in local Zakat committees, introduced with the involvement of Ulema or imam of the local mosque, can help in reducing political influence.

On the other hand, in screening for marriage assistance, the age limit should be extended. Some women get married much later in life as they have to take care of their parents and siblings, but they are still poor in their mid-30s or early 40s.

Lastly, in order to reduce political influence, diversity in local Zakat committee should be introduced with involvement of Ulema or imam of the local mosque. Such is the practice in Malaysia and Brunei as well. The more diverse the local Zakat committee, the less will be the chances of favoritism.

The district Zakat officer should ask in writing from each Khateeb/Imam of mosque or the administrative committee of a mosque to give their office names of five to ten people who are regular in offering prayers in the same mosque and are known to be pious and honest people of good reputation in the community. In addition to these people, the district Zakat officer should ask for the names and details of those who are relatively well-off, who have some administrative experience and who are living a retired life. Such persons have the time to volunteer and they do not have need for funds for themselves. With administrative experience, they also have the required skills to perform the required role in community.

Once the district Zakat officer receives the names of such people from each mosque, which falls in the jurisdictions of local Zakat committee, then district Zakat officer or his nominee should meet all such people in the same mosque. The district Zakat officer or his nominee should brief them about the work of local Zakat committee and then give them ballot and ask them to write the name of a person, whom they consider better among them for this task.

However, none of the persons should be allowed to write their own names. Everyone has to write the name of others, whom he considers relatively better than himself. The one who receives the highest number of recommendations/votes should be made member of the local Zakat committee. District Zakat officer or his nominee will declare the name of such person while there is no need to announce the number of received votes by each.

There will be a need for training of district Zakat officers to carry out this process in practice. Once all such exercise is done in all mosques falling in the jurisdiction of local Zakat committee, the office of district Zakat officer should issue notification of the formation of local Zakat committee. The wife (if alive) of each member could be declared member of local Zakat committee by default so that every member can take help from her, during shortlisting process of Zakat beneficiary.

District Zakat officer or his nominee, should follow the same process for the selection of chairman of local Zakat committee after calling the first meeting of local Zakat committee members from every mosque. If there are multiple mosques in the locality, then one member from two or three mosques can be selected. Likewise, if there are fewer mosques, then two or three members from one mosque can be selected. In this manner, the local Zakat committee will become non-political. It will also ensure that people in the committee are from the same area and have good moral character and reputation. It will increase the confidence and trust level of people.

In future, if the scale of collection is to be increased and also from grassroots level, then it is necessary to have members in local Zakat committee who are well versed in Zakat rules and jurisprudence. Ulema and imam of mosques are in a good position to offer assistance to people in Zakat assessment. They are already doing this work for people on voluntary basis. What is needed is to recognize their role and formalize their engagement in a structured way.

### 6.1.3. Recommendations in Zakat Disbursement

#### 6.1.3.1. Using Digital and Fast Mediums of Disbursement

Currently, local Zakat committees are engaged in not only eligibility checking process, but also in disbursement process. With the increased use of digital payments and digital banking, the disbursement function can be simplified by reducing the role of local Zakat committees.

In place of order cheque, which still has shoe leather and transaction cost, it is better to utilize mobile banking and Biometric Verification System based digital payment platforms, such as easypaisa, Raast, etc. This will reduce chances of corruption and bring transparency into the system.

Use of mobile banking and BVS, like easypaisa, Raast, etc. can help in reducing chances of corruption and ensuring transparency.

The possibility of issuing cheques directly from district Zakat committee to beneficiaries can be explored. In this way, the third layer will not get involved and it will save time and inefficiencies.

Using crossed cheques for marriage assistance creates hindrances for the family. Women may not have a bank account and opening an account after receiving the cheque can be a tedious and time-taking process. Hence, in such cases, order cheques could be used.

#### 6.1.3.2. Introducing Synergies in Programs – Graduation-Based Social Protection

Creating synergies within and across programs can help in complementing the impact of programs and provide multiple solutions to the beneficiaries. For instance, productive Zakat can be given to small growers and their production can be purchased by the Zakat Department to distribute food packages among the poor.

Likewise, productive Zakat can be given in the form of tools, machinery and business assets. Little cash assistance does no good to poor other than feeding them for a brief time period. It is insufficient in itself to ensure socio-economic mobility. Rather, it makes people trapped in the system with gradual loss of capacity and motivation to work. There are examples from East Asia and also Bangladesh that entrepreneurship is a useful vehicle to ensure socio-economic mobility.

The production or services thus generated from the business assets can be purchased by the Zakat Department to distribute among the needy people. For instance, giving sewing machines to female Mustahiq. They can be organized as a group to prepare school uniforms for particular schools where there are students of poor people. The uniforms so produced can be purchased by the Zakat Department which can then provide these to deserving students.

As another example of synergy, in place of marriage allowance, mass marriages can be sponsored where public crowdfunding could be sought through event crowdfunding model.

### 6.1.3.3. Introducing Wakalah Program

Social intermediation is also an important economic function. Social intermediaries like philanthropic or welfare organizations pool pro-social savings from donors and distribute them among the have-nots. In a social setup where several private NGOs perform this function, these organizations compete for the funds.

In Pakistan, Zakat collection and disbursement is by and large decentralized. It is estimated that as much as Rs. 500 billion to Rs. 700 billion Zakat and charity is given annually by Pakistanis domestically and abroad while the collection by the government is just 1% to 2% of that value.

In order to strengthen Zakat collection and disbursement through the government-run Zakat system, the government may introduce a Wakalah scheme to create complementarity between the collection efforts of private NGOs and the government. Malaysia has introduced such a Wakalah program.

Approved institutions can be given permission to assess and receive Zakat from the people, but report and transfer it to the government. Government will return back a certain percentage of funds to these institutions so that they can disburse the funds as per the stipulated conditions and guidelines. Malaysia also allows Wakalah institutions to receive Amil funds for their operational costs. Such a Wakalah program can help in creating complementarity rather than competition among the social intermediaries for sourcing the charitable funds.

To strengthen Zakat collection and disbursement through the government-run Zakat system, the government may introduce a Wakalah scheme to create complementarity between the collection efforts of private NGOs and the government.

Besides collection, Wakalah program can also be used in disbursement whereby individuals and institutions giving their Zakat to the government can specify beneficiary institutions and individuals to whom Zakat shall be paid. Zakat Department can allow payment of up to 50% of the Zakat received to the identified beneficiaries. This can help in creating penetration in social intermediation function without disrupting the role of other social intermediaries and creating unnecessary competition.

### 6.1.3.4. Documenting the Economy for Effective Targeting and Profiling

The government at a strategic level should look to bring all data in one place including demographic data about an individual and the contracts of sale, purchase, lease, investment and loan he has entered into so that it leads to the development of unified or single registry by integrating various program levels and CVRS databases. It will help in reducing data collection and verification cost which is vital in effective and efficient targeting.



Meeting eligibility requirements and documentation also rests on efficient operations of NADRA and all relevant agencies and departments from whom documentation is required to prove disability and other inopportune circumstances.

Therefore, efficiency, one-window operation and quick turnaround time should be ensured in facilitating poor people who take great pains to come to government departments for verification and documentation.

## 6.2. Recommendations for Ushr Management

### 6.2.1. Amendments in the Legal Framework

In Zakat and Ushr Act, 2011, it is stated in clause 5 that “Provided that if any plot of land is used principally for growing one crop and a small portion thereof, not exceeding one-fourth of an acre, is used for growing another crop, Ushr shall not be charged in respect of the produce of such small portion.”

It must be noted that in Hanafi Fiqh, there is no such exemption on produce of land. 25% of a bigger plot maybe a large value as compared to 25% of a medium or small sized plot. Plot size is not specified in the statement of the law.

The law states that Ushr shall be collected in cash. Keeping in view the primitive nature of farming in some parts of the region, farmers should be allowed to pay in kind, especially for crops which are not perishable in short-term. Nonetheless, it will create issues in collection for the government. It is important that neither the government nor the farmer should suffer from the loss of value in liquidating the crops in cash at the time of collection. Receiving Ushr in kind can also allow the distribution of food packages to the Mustaheqeen. This is the practice followed in the Kedah State of Malaysia.

In the Second Schedule of Zakat and Ushr Act, 2011, it is stated that on agricultural yield other than the tenant’s share, “One-fourth of the value of produce is allowed as an allowance for expenses on production”. This apparently is based on the law of the land, not of Shari’ah.

This clause may be revisited from the Islamic Fiqh perspective to justify the basis of this exemption. Expenses on production cannot be adjusted against the value of produce subject to Ushr. Only the direct marketing expenses, such as costs of packing, loading and transportation can be adjusted.

### 6.2.2. Using Surveys for Assessment

In the case of Ushr, if average productivity yield in an area is used to determine Ushr liability, then it can help in assessment by applying the average yield to a particular cropping area whose size is easily measurable, but its yield is not measurable at the time of harvest or afterwards. Sometimes, even the owner is not confirmed about actual productivity and may keep no documentation.

In allowing for exceptions, an appeal or review mechanism can be introduced. Clause 3 of Section 6 of KP Zakat and Ushr Act, 2011 has provision for grievance redressal. Furthermore, third party evaluation can be introduced to handle and verify the grievances. Appeals process may involve nominal fees as a deterrent against people who are simply trying their luck. Fees will be refunded after the farmer is able to provide evidence that his crop was lower than average or was lost in some catastrophic event. Currently, even the internal review (other than third party evaluation) requires 50% advance payment of the assessed amount of Ushr liability before the appeal can be even admitted for further inquiry.

### 6.2.3. Assessing Ushr by Government as Monopsony

It is also possible to charge Ushr or Nisf Ushr at the point of sale if the government is monopsony in buying agricultural commodities. The government often procures food crops from farmers at support prices. At the time of purchase, Ushr in value can be deducted at source.

A concern may be raised that if farmers are going to be charged Ushr in transactions, they will look to sell their output in the open market. Hence, it is important to make selling of products to the government an attractive proposition for the farmer by introducing certain incentives which are discussed next.

### 6.2.4. Introducing Incentives for Ushr Payment to the Government

Some incentives should be in place to allow farmers to pay Ushr to the government. These possible incentives could take the following forms:

#### 6.2.4.1. Linking Market Access with Ushr

Ushr payers can have first access to sell output to the government. If the government guarantees procurement at support prices which are competitive with the market, then farmers will be willing to sell to the government and avoid the exploitation of middlemen and situation of deflation when there is a glut.

In the transitional period, the government may proceed to procure crops from all farmers, but offer higher support price and larger quotas to farmers who pay Ushr. It will encourage people to pay Ushr to the government in order to sell more output at higher price.

Coupons and passes to enter roadshows and exhibitions for greater market access and outreach can be offered to registered Ushr payers.

#### 6.2.4.2. Linking Subsidies with Ushr

The government can introduce a condition that only registered Ushr payers will be able to get subsidies in buying fertilizer, pesticides and insecticides.

Likewise, the government can engage with banks and Takaful operators for agri-financing and crop Takaful. The government can partly support the cost of financing like it does for clients in export refinance scheme. The Islamic alternative of export refinance scheme is in practice in banking. Hence, a similar scheme can be introduced for those farmers who are registered Ushr payers.

Likewise, Takaful operators can be engaged to provide crop Takaful at competitive and attractive Tabarru (donation) contributions to the registered Ushr payers. Part of the contribution due on the part of the Ushr payer can be shared by the government or can be topped up by the government to increase the coverage.

#### 6.2.4.3. Tax Incentives for Ushr Payers

Rebates can be introduced for indirect taxes paid in purchase of inputs, such as tractors, fertilizers, insecticides and pesticides.

Adjustment of tax liability on agricultural income can be an important incentive. Exemption given in clause (b) of Section 24 of the Zakat and Ushr Act, 2011 should be popularized further to induce Ushr payment to the government.

#### 6.2.5. Strengthening Land Records

It is important to improve land records in order to ascertain ownership. It is vital to ensure that incidence of Ushr is where it should be. For this purpose, the district and provincial governments have to conduct meticulous surveys. The government's recent efforts in digitizing land records is also going to complement such endeavors. A due date should be publicly announced within which people owning farmland must submit application for proper documentation of their landholdings.

The deterrent against avoidance should be strong penalties and cessation of property if not registered. At the time and place of buying farm output and selling farm inputs, documentation should be made necessary. Incentives for compliance and penalties for non-compliance should be introduced to discourage avoidance of coming in the net of formal documentation.

It is important to build trust of the people that they would not be double charged. Rather, it must be shown through public announcements and explanation that by disclosing their landholdings and paying Ushr, they will have tax savings. The challenge is that disincentives and deterrents should be strong enough to ensure that people do not try to avoid documentation.

Consistent and credible policy together with prudence to not overburden farmers is necessary. Incentives need to be made attractive enough. In the initial stages, the focus should be on bringing agricultural output in documentary net and establishing ownership records. If focus is put more on generating as much revenues as possible in a short period of time, then people will hesitate and will not cooperate.

## 6.3. Policy Recommendations on Waqf

### 6.3.1. Allowing Private Sector Engagement in Waqf Management

To encourage the creation of Waqf other than in dormant real estate, private entities should be incentivized to establish, manage and administer Waqf with the role of Chief Administrator being a monitor and supervisor. The Chief Administrator can oversee the preservation of Waqf assets, but the development function should rest with independent managers who have the authority to make decisions.

To enhance and uplift the Waqf institution, different types of Waqf, such as property, family, cash, and corporate should be legally recognizable and registered.

The role of Chief Administrator should be to monitor and supervise, whereas the management and administration should be allowed to be handled by private entities in private Waqf. Abrupt appropriation of the Waqf assets by the government would further dampen the confidence of people who want to engage in private social savings and decentralized provision of social safety nets through Waqf.

### 6.3.2. Active Waqf Management for Preservation and Growth

There should be a balance between preservation and development. To encourage private participation, there should be flexibility in the use of Waqf assets for investment in the form of leasing and financial investments. At the same time, it is important to have risk management guidelines to ensure the preservation of Waqf assets.

Provisions should be added in the existing laws regarding ‘Istibdal’ (substitution) of Waqf assets in order to revive the old Waqf assets, revitalize the existing ones and to ensure sustainable existence and utility of Waqf assets. Istibdal on the premise of commercial viability and enhanced beneficial use can also be allowed under regulatory and compliance surveillance. The real purpose and essence of avoiding usurpation of property can be ensured even with Istibdal since ownership would nonetheless still remain non-private after Istibdal.

### 6.3.3. Encouraging Corporate Waqf

It is important to provide tax incentives to engage more people and corporations towards establishing Waqf. Corporations which engage in corporate philanthropy can effectively establish Corporate Waqf. The contributions to these Waqf by individual and corporate donors should be made eligible for tax credit like it is the case with other recognized institutions in Section 61 of the Income Tax Ordinance, 2001.

Corporate Waqf should be allowed to be established as a corporation limited by guarantee. This practice is followed in Malaysia where Johor Corporation, Waqf-An-Nur and Auqaf Holdings are some of the established Corporate Waqf. They are registered as ‘corporation limited by guarantee’ by the Securities Commission.

The legal framework must not put an undue restriction on the creation of new Waqf either by the individuals or by the organizations in order to encourage Corporate Waqf which can help in achieving scale and effective mobilization of funds and management of funds.

#### 6.3.4. Tax Incentives for Creating Waqf

If a donor dedicates real estate to an existing Waqf or to establish a new Waqf, the taxes related to registration and transfer of property shall be exempted. Furthermore, tax amnesty scheme can also incorporate the Waqf institution by allowing exemption from previous taxes on the real estate that is donated as Waqf.

#### 6.3.5. Recognition of Different Waqf in Legal Framework

The current Waqf laws in Pakistan only stipulate the role of Waqf administration as gatekeeping of existing historical properties which due to some reason have come under the purview of Ministry of Religious Affairs, such as shrines, mosques, Madrasa, etc.

Waqf law should provide a comprehensive definition of Waqf. It must explicitly cover various types of Waqf such as:

- ❖ Property Waqf
- ❖ Family Waqf
- ❖ Cash Waqf
- ❖ Corporate Waqf

The legal framework should not restrict the definition of the endowed asset to immovable tangible assets only, such as real estate, but should also explicitly recognize movable, financial and intangible assets, e.g. cash, stocks, gold, financial securities, equipment and transportation vehicles.

#### 6.3.6. Recognition of Cash Waqf in Legal Framework

Cash Waqf is recognized in different Muslim countries. It has been recognized in Malaysia since 2007. Rationale for Cash Waqf from juristic perspective is that Waqf asset or capital needs to be preserved for its perpetual existence. Hence, capital in Cash Waqf itself should not be used in providing benefits and services to the beneficiaries, but the proceeds of cash received in Cash Waqf can be invested in low-risk low-return Shari'ah-compliant investment options in order to generate returns. Such returns on investments can be used to provide benefits and welfare services to the beneficiaries.

Another important use of Cash Waqf is to allow crowdfunding for purchase or provision of expensive assets and infrastructure which cannot be funded by any single person. But, through Cash Waqf, donations can be pooled from a diverse cross section of people which can allow the accumulation of enough capital to purchase or establish the necessary infrastructure for

welfare services. Hence, due to its economic rationale and potential, Cash Waqf should be introduced in the legal framework.

#### 6.3.7. Transparency in Management and Reporting

Laws must make it compulsory to have transparent and honest reporting of financials. Punitive actions should be taken against the abuse or usurpation of assets by the trustees and in this regard, financial penalties should be complemented with physical punishments to act as strong deterrents.

#### 6.3.8. Joint Ventures for Waqf Development

Islamic banks can facilitate the development of old Waqf assets by way of diminishing Musharakah, sale and leaseback, and Istisna in order to rebuild and renovate Waqf property for improved post-financing valuation as commercial buildings.

State Bank should subsidize the financing cost of building and renovating old Waqf assets by employing Islamic banks for financing the building and renovation cost. The subsidy in financing cost will pay off in terms of post-financing valuation of Waqf property as commercial buildings.

Malaysia has successfully used Waqf for building commercial malls and hotels, such as Pantai Puteri (Malacca), Regency Seri Warisan (Perak), Grand Puteri (Terengganu) and Klana Beach Resort (Negeri Sembilan). Such activity will increase employment in construction sector which is interlinked with many other sectors.

#### 6.3.9. Diversify Revenue Streams

It is important to diversify and extend revenue streams to allow larger scale of extending socio-economic and welfare services to the beneficiaries in society.

Currently, the revenues come in the form of rents of shops, farmland, houses, cashbox donations, contract fees and return on passive financial investments.

The revenues from these streams can be enhanced by developing the Waqf properties. For instance, converting a barren piece of land into residential apartments, shopping complexes and business centers. Carving out the land to allow fragmentation and then to develop the land can help in raising the value of Waqf property, create employment opportunities, create economic activities and in turn raise the rental income that can be generated.

## Chapter 7

# Possible Models to Deliver Social Protection Under Islamic Social Finance

This chapter discusses some other alternative models of delivering social financial services for social protection through Islamic social finance tools. These models may require some fundamental changes and require more time for implementation. However, there are merits and advantages in these delivery mechanisms as discussed. The details of such possible models are given below.

### 7.1. Mosque-Based Waqf Places for Community Health Services

Every Muslim community has a mosque, and in some communities, there are more than one.

Social service delivery requires human resource. To reduce the cost of engaging human resources, volunteers are always handy. One possible model to provide basic medical services at the grassroots level in underdeveloped regions without nearby hospitals is to engage volunteer medical officers who can volunteer few hours every week.

In almost every locality, there are retired people from health-related fields, and they have the time and willingness to serve their people without a fee. What they need is facilitation, acknowledgement, empowerment and an enabling environment.

They cannot turn their houses into health centers as this would disturb privacy of their family life. To overcome the issue of place of delivery of health services, mosque can play a major role in matching those who are needy with those who are willing to serve.

For example, there are 100 to 130 families (households) living in the area around a mosque. A retired medical officer in the same area can be engaged who is willing to serve this community from 9 am to 12 pm. He needs a place where he can attend the patients. If this medical officer is provided a place, then he can help voluntarily all these people on a regular basis. If some part inside a mosque, which is free during this time, is provided to the medical officer, then he will be in a better position to serve the needy.

In case someone offers a place other than mosque for this purpose, then the same place can be declared Waqf and be given under the supervision of mosque. Once this model starts working, then many people in Pakistan can be provided basic medical attention.

### 7.1.1. Operational Delivery Mechanism

This activity can be started as a case study through an executive order within the current legal framework of Zakat Department. It does not require any change in law and have no additional financial burden on Zakat Department.

Initially, Provincial Zakat Council has to allow district Zakat officers/chairman to identify mosques where such activity is possible. District Zakat officer/chairman can then ask local Zakat committee to find such a mosque. Once a mosque is shortlisted and willingness is taken from all stakeholders (mosque committee, medical officer), then local Zakat committee chairman can start this activity.

A medical officer will come to the mosque or other designated place and inspect the patients in the given time. Other resources, such as attendant/staff can also be provided by the mosque committee. After providing basic facilities, Zakat Department can then ask the doctor to run the activity independently.

After doing such initial level activity, the project can be expanded slowly and gradually to other areas and a time may come when all mosques will have such centers for helping poor and excluded people. Other inputs required for such activity like medicines can also be furnished by crowdfunding in the same area. People give Zakat to religious schools by witnessing that they provide a social service of educating children. Hence, if they see that a health clinic is being organized in mosque building, then they will be willing to provide their charitable funds to this social cause. The role of imam is also important in encouraging people to come forward and help in health-related service delivery by providing donations generously. In many cases, the endorsement by imam also plays a positive role in enhancing trust among people.

In this manner, a whole ecosystem can be developed where the need for technical human resources, donor community and place of service delivery will come together to ensure availability of health services for rural and suburban communities at grassroots level.

However, it must be noted that Waqf needs transfer of ownership from Waqif to the Waqf Department. To reduce complexity, if some Waqif wants to donate place and/or funds for construction of smart health clinic, then such a place or infrastructure can be donated to a registered mosque under Waqf Department of the government and then management committee of the mosque should be allowed to use the Waqf property for providing the service and facility to the community.

### 7.1.2. Points to Consider in Implementation

It is possible that patients from other areas may start coming to this place, thus making the activity unsustainable for the medical officer due to overcrowding. However, this will be a short-term issue and the solution is that the number of patients per day can be limited by mosque committee to the local patients only. Attendant of the medical officer will first make a list of the patients per day and then call the medical officer. Once the model becomes



successful, then it could be replicated in other mosques/areas. This will solve the issue of overcrowding as there will be little incentive for a poor person to visit other mosques.

Another issue is that women and children also need health attention. Thus, the mosques shortlisted for this model in initial experimental phase should be spacious enough and have a non-praying area where women, children and some basic furniture and tools can be adjusted. Timings should also be such that the mosque does not have classes or prayers during that time. Furthermore, solar panels can be used to manage the electricity cost.

## 7.2. Sadqa P2P Crowdfunding Platforms

It is a common observation that there are many people in society who are willing to take care of various needs of the poor, including hunger. Rather, enthusiasm for feeding the hungry prevails on a large scale in society, but people are hesitant to come forward and feed the hungry, as they think that such people may permanently become dependent on them. In other words, they fear the transaction cost of feeding a hungry. Likewise, they fear that if they help a poor person, many other poor persons will start coming and may bother them.

These transaction costs of helping others restrict the mobilization of funds from the giver to the needy. Collecting information about the deserving people in society has a cost.

It can be said that people want to help people (P2P) but the cost of helping restricts many people from doing so. In this regard, some intermediary/platform is required to collect funds from people who are willing to give and pass on to those who are needy and willing to accept. The provision of such platform will facilitate the help of many deserving people without putting any burden on the government. In this regard, mosque can become a very good platform for matching the needy with the donors.

### 7.2.1. Operational Delivery Mechanism

Zakat Department has to start the drive of voluntary registration of mosque. Those willing to register should get a registration certificate from district Zakat office. Official of Zakat Department at province level should seek legal process from relevant authorities of online platforms, such as easypaisa and JazzCash, to offer registered mosques a mobile account based on the registration certificate.

Telecom companies will have to issue new SIM card to registered mosque in the name of someone recommended by the mosque committee. The same SIM card can be used for opening a mobile account (easypaisa, JazzCash, etc.).

In addition, Zakat Department can seek permission for each registered mosque to open an account in any scheduled bank of Pakistan. Once each mosque has accounts, then anyone can submit or transfer donation to these accounts for helping the poor, living in the jurisdiction of the same mosque.

The donor can tell the mosque committee that the given donation is for some specific needy person. The committee member can also display the list of needs of poor inside a mosque (without mentioning names) along with the required amount. A donor can check the list and transfer the required money into the account and inform Khateeb/mosque committee about the transaction.

Such provision of collection of donations will drop the transaction cost of direct help and facilitate everyone in the society to help needy people, living around them, in a respectable manner. Once each mosque is legally provided such facility, then over time, the system of P2P will become stronger and every mosque would like to join the registration process voluntarily. This will also resolve the issue of registration of mosques in Pakistan as the process involves incentives for mosques.

### 7.2.2. Points to Consider in Implementation

One of the possible issues in this process is the audit of the funds. For this purpose, all transactions from the bank account should be made via crossed cheques. Likewise, all transfers should be made online from mobile accounts. The statement of both such accounts will have to be verified by the mosque committee. Next, a verified statement signed by the Khateeb and all committee members should be submitted to the district Zakat office after six months.

Another issue is the incentive for Khateeb as most of them are poor. The solution is that some fraction of the collected amount be reserved as a salary for them. It is worth mentioning that the same process is followed in Kedah State of Malaysia where the Khateeb is given 5% of the Zakat collected by the mosque. Such payment is given to them under the head of Amileen Zakat. The other solution is that the basic needs of the Khateeb should be fulfilled from the collected funds. However, the cost of fulfilling the needs should not exceed 5% to 10% of the collected funds.

## 7.3. Voluntary E-Zakat Collection and Disbursement Through Crowdfunding

As mentioned earlier, there are various mosques in the jurisdiction of each local Zakat committee. The members of local Zakat committee should meet with imam/Khateeb and committee members of all mosques and take them into confidence for raising Zakat funds (not general donations) to be used for the needy living in the same area.

Next, local Zakat committee can start a Zakat collection campaign with the support of all mosques falling in the jurisdiction of the committee. All collected Zakat will be deposited in the account of local Zakat committee and can be utilized for Guzara allowance. All such funds can be audited in the same way as the other funds.

In addition, all funds, whether they are coming from province or local Zakat committee, should be disbursed by using online mobile payment system such as easypaisa, JazzCash, etc. The task

of the chairman of LZC would be provision of a list of beneficiaries along with account number to district Zakat officer.

After proper administrative procedure, the funds would be transferred to mobile banking platform such as Telenor/easypaisa, which will then disburse the funds as per the given list into the account of beneficiaries. It is worth mentioning that online transfer via mobile banking mechanism has already been adopted by Zakat Department in Punjab province.

### 7.3.1. Points to Consider in Implementation

In the presence of P2P platform, people might be reluctant to give and deposit Zakat in the account of local Zakat committee. The solution is that currently P2P platform at mosque level is not available. Till the time of achieving P2P platform, this system can be tested as a case study. In case it works and attracts the confidence of people, then the same account can be used for P2P platform. In such case, the model of Malaysia can be adopted under which each mosque has a reference code and all or fraction of the funds collected through such reference code are used with the permission of the Khateeb/imam for meeting the needs of poor in the area of jurisdiction of the mosque. Likewise, some fraction of the collected amount is given to Khateeb under the head of Amileen Zakat.

## 7.4. Mosque-Based Skills Development

There are many people, both men and women, in a society who are living a retired life. Each has some skills and experience and are willing to transfer it to the younger generation of the same community without any monetary benefits.

However, they lack a place and mechanism to meet these young people and share their experiences. Mosque can be one such desirable place. If mosques having classrooms allow the meeting of these experienced people with the youth, the latter might learn many skills and start earning independently.

If mosque committee cannot provide a place for such activities, then they can ask someone in the same area who owns a private school/large property/guest rooms, etc. to facilitate such meetings.

The only thing a mosque committee needs is to own this process of facilitation of two sides and provide a place inside or outside the mosque. If mosques arrange such activities for the betterment of excluded people, then the P2P platform of mosques will attract more funds as the people will realize that mosque is taking ownership of the issues of community.

Currently, most of the mosques are owning little about the issues of community, thus playing a limited role in solving pressing issues of the poor people. Such facilitation will enhance the role of mosques in solving the issues of excluded people in society and their financial development.

## 7.5. Integrated Microfinance for Social and Financial Development

Many people in society keep extra money in current accounts with banks. All scheduled banks do not offer any return on current accounts to account holders. However, when banks use these funds by making short- or long-term investment, etc., they earn profit/interest.

If State Bank of Pakistan makes it compulsory for all scheduled and microfinance banks to use some fraction of the current account funds for soft loan to those who are interested to initiate small businesses, then many people will be able to initiate new businesses.

However, the banks fear default. In this case the guarantee of such people can be provided by the chairman of local Zakat committee on the recommendation of two members of local Zakat committee. If chairman of local Zakat committee recommends someone, then the relevant branch of a bank should consider that person for soft loan of small amount ranging from Rs. 20,000 to Rs. 50,000. This soft loan may be provided for up to six months. In this way, the money of the local people will be used for the benefit of the needy local entrepreneurs. This will also enable the banking sector to fulfil their corporate responsibility. The guarantee by the members of local Zakat committee will put social pressure on the recipients of the soft loan, hence the probability of default will be either zero or negligible.

However, if some default occurs due to unavoidable reasons, then local Zakat committee can raise funds within the community through P2P platform for such person and return the loan to the bank on behalf of such person. In this way, banks, local Zakat committee and local account holders will be helping the needy people of their community and thus playing a role in the development of the community.

Currently, the link between local Zakat committee and scheduled banks is absent, and every institution is working in isolation. Thus, on average, the development speed is slow, and the number of excluded people is multiplying. Through this mechanism, the number of excluded people can be decreased over time by creating a link of local Zakat committee with other financial institutions.

The possible issue in this case is moral hazard on the side of user of funds. Once, a borrower realizes that community will return the loan in case of default, then he might become careless in use of such loan and do willful default. This issue can be solved if the borrower is made to realize that he will never be recommended in future for any such loan if he defaults. As business is a regular phenomenon and one needs finance repeatedly, hence, this threat will keep him away from willful default.

## 7.6. Role of Mosque in Creating Synergies with Other Programs

Mosques can play a role in helping a national level institution to help the needy. For this, it is worthwhile to look at details of the Ehsaas Roshan Riayat program of Government of Pakistan under Ministry of Poverty Alleviation and Social Safety. The former prime minister of Pakistan announced Ehsaas Roshan Riayat program on November 3, 2021. Under this program a

registered family was provided subsidy of Rs. 1,000 per month on the purchase of flour, oil, and pulses.

One of the key components of this program is selection criterion. The available information mentions that the government conducted a survey across the country and families found eligible were able to benefit from this program. All aspirants sent their CNIC number to 8171 and the details of such persons were counterchecked in the database of eligible families. They were offered subsidized *rashan* if found in the list, otherwise, they were sent a message of regret.

This program has two major issues – high cost of reaching out to deserving families and static approach, i.e. lack of dynamism. The collection of information about the eligible person/family is very costly and a one-time survey might not be enough for sorting out eligible families as this needs repeated surveys. But carrying out survey on regular basis with short intervals is non-manageable due to high cost. On the other hand, without doing repeated surveys, it cannot be known with certainty whether some eligible family is still poor or not. This created a dilemma. Efficiency requires repeated survey, while the cost of repeated survey is making it unachievable. Hence, underachievement results as a consequence of the inefficiency of cost of collecting new information or the inefficiency of relying on old information.

How to solve the issue of collecting repeated information with low level of transaction cost? For this purpose, mosque-based Mawakhat model is suggested. Under this model, the Khateeb or committee of a mosque will be given the task to identify poor families around the mosque via questionnaire to be given by local Zakat committee.

It has already been mentioned that almost each mosque in Pakistan has an administrative committee from the local population. Such administrative bodies have information about almost all families living around the mosque. So, they can easily provide information about the total number of eligible families in the surroundings of that mosque. This information can be provided on the same questionnaire the government is using along with CNIC number and comments if required. For example, the mosque committee can provide information that who among the poor are suffering from abject poverty and hunger.

Such information can be provided voluntarily by each mosque committee or with a very low level of cost. After receiving such information, local Zakat committee can target only those families which fall among the poor in the provided list of a mosque committee.

To double check the validity of such information, audit team of district Zakat office can conduct a random check by doing detailed survey of some families. This will provide opportunity to the authorities to validate the information provided by the mosque committee.

Such validation will cost little but will remove any doubt about the lists. In addition, the collection of information about the poor families will make this process more dynamic. As the cost of collection is negligible for the administrative committee, so they can update the list on a regular basis after some interval (six months or a year).

As mentioned earlier, the collection of such information via national level survey is costly and requires a huge budget. In addition, there is no system of double checking until another survey is conducted, making the cost even higher. The collection of information based on mosque-based Mawakhat model would solve the issues of cost and dynamism along with the provision of double checking.

### 7.6.1. Points to Consider in Implementation

One possible issue in this arrangement is training of local people about the nature of required questionnaire. In addition, repeated survey will require some cost even if it is low. The repeated provision of covering such cost might be difficult for the government. Monetary cost of such activity would be negligible if performed voluntarily. Still, some fraction of the funds from P2P platform can be utilized for this purpose in case of shortfall. The reason is that support in the efforts for enabling the government to divert resources towards the deserving is also a charity. Hence, allocating some resources from P2P platform should not be an issue.

Regarding training, the government can first train some master trainers at national level, and they can then invite one volunteer from each mosque for further training. This volunteer can then train more volunteers at mosque level. These volunteers can then fill any kind of questionnaire in a professional way. In addition, such a pool of people can be utilized in any disaster/urgency, such as flood and earthquake, for conducting accurate surveys about damages to families at local level for sharing with the government. Thus, the provincial or federal government will have accurate information about the human and financial losses of a disaster within the shortest possible time.

## 7.7. Embedding Islamic Social Finance in Sehat Sahulat Card

Islamic social finance can be embedded and integrated in beefing up the Sehat Sahulat Card program. Following three proposals came out of discussions with study group members and meeting with chairman of Sehat Sahulat Card program. These are:

### 7.7.1. Using Takaful

The first proposal relates to the use of Takaful instead of conventional insurance. Conventional insurance is considered impermissible due to the involvement of Riba, Gharar and Maysir. If premiums are sourced as voluntary donations and investments are made only in Shari'ah-compliant instruments, then this system can be made Shari'ah-compliant.

One of the major reasons for involuntary financial exclusion in Pakistan is that most financial services are interest-based whereas majority of the population is Muslim and wants to avoid the element of interest.

Insurance coverage is not a pressing need all the time like hunger or thirst. So, if some alternative is not compliant with faith and faith conscious people also do not face dire circumstance which necessitates its use, then most of them do not opt for insurance. Pakistan

has one of the lowest insurance penetration ratios in the world. People with huge real estate and financial wealth may still have no insurance coverage primarily because they wish to avoid conventional insurance which is not compliant with Islamic principles.

Hence, the Sehat Sahulat program can be redesigned to comply with Islamic principles. In this regard, State Life Insurance Corporation already has Takaful operations. Thus, the transition requires using a different product rather than the conventional insurance.

If the system is designed and branded as compliant with Islamic principles, then a lot more people will not even hesitate to contribute voluntary donations (as an alternative to premiums) in order to get themselves covered through an Islamic alternative.

### 7.7.2. Using Social Crowdfunding

In Pakistan's health sector in particular, there are many examples of institutions establishing and scaling purely from social crowdfunding. Indus Hospital, Sindh Institute of Urology & Transplantation, Shaukat Khanum Cancer Hospital and many other such institutions are working through crowdfunding.

These institutions depend majorly on donations. They source Sadqa and Zakat funds through various campaigns. Such mobilization can also be adopted for Sehat Sahulat Card. If Takaful model is used, it is hoped that there will be greater participation of people in donating to it on the premise that it is a Shari'ah-compliant scheme.

### 7.7.3. Building Smart Hospitals on Waqf Property

To provide healthcare services to millions of enrolled patients, the Sehat Sahulat Card program will require additional infrastructure and enhancing the capacity of existing healthcare system.

New smart hospitals need to be built in communities, especially in rural areas and small cities. For such smart hospitals, property Waqf can be used to dedicate land for establishing smart hospitals.

Property Waqf can be used straight away if some individual or institutional Waqif or the government itself wants to dedicate land for this purpose. Else, if crowdfunding is required, then even Cash Waqf donations can be pooled to buy the land for building a hospital.

In construction, public-private model can also be used. Constructors or healthcare service providers will wish to venture in providing healthcare services knowing that the government has earmarked funds for Sehat Sahulat Card. With the right mix of tax and duty incentives along with subsidies, a build, operate and transfer model or long-term lease contracts can be introduced to cover and spread cost.



**Institute of Policy Studies**  
Islamabad

**Institute of Policy Studies** | Nasr Chambers, Plot 1, Commercial Centre, MPCHS, E-11/3, Islamabad.



+92-051-8438391-3



+92-051-8438390



info@ips.net.pk



ips.org.pk | ipsurdu.com



InstituteOfPolicyStudiesPakistan



IPS\_1979



IPSTV



Institute of Policy Studies, Islamabad