

**IFSB WORKING PAPER SERIES**

**WP-29/12/2023**

**REGULATORY PRACTICES IN ISLAMIC SOCIAL  
FINANCE**

**DECEMBER 2023**



**ISLAMIC FINANCIAL  
SERVICES BOARD**

**WP-29/12/2023**

**REGULATORY PRACTICES IN ISLAMIC SOCIAL  
FINANCE**

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**December 2023**

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The authors would like to acknowledge the immense contribution of IFSB Fellows, Bilkis Lawal Shuaibu and Mohammed Hamza Ghaouri in the drafting of the paper. This working paper has benefited from the feedback and guidance provided by the Acting Assistant Secretary-General, Aminath Amany Ahmed and the members of the Standards Development and Research Department of the IFSB and members of the IFSB Technical Committee who reviewed the draft paper. The authors are grateful to all IFSB members who participated in the survey, and for providing useful comments on the draft paper during members' consultation.

**Published by: Islamic Financial Services Board**

Level 5, Sasana Kijang, Bank Negara Malaysia

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## **ABSTRACT**

The paper's main objective is to comprehensively discuss and compare the regulatory and supervisory practices in Islamic Social Finance (ISF) across jurisdictions. The paper highlights the vital role of ISF as a means towards socio-economic inclusion as well as several challenges hindering its potential impact and regulation. Pertinent issues are covered, including but not limited to the difficulty in conceptualising ISF due to varying practices across jurisdictions, concerns about the significant financial transactions in ISF institutions, and the risk of mission drift leading to commercialisation of social welfare promotion. Based on a review of regulations and relevant documents complemented by a survey questionnaire to gather valuable insights, the paper's findings provide a basis for a better understanding and any need for future work in the ISF domain. It offers recommendations to overcome challenges faced by regulatory and supervisory authorities, aiming to improve existing practices related to ISF. The findings should inform the future work of the IFSB in related areas.

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## ABBREVIATIONS

ASEAN	Association of South-East Asian Nations
AML	Anti-Money Laundering
BAZNAS	Badan Amil Zakat Nasional
BWI	Badan Wakaf Indonesia
CFT	Combating the Financing of Terrorism
CMA	Capital Market Authority
ETFs	Exchange-Traded Funds
ESG	Environmental, social and governance
FATF	Financial Action Task Force
ICM	Islamic Capital Market
IsDB	Islamic Development Bank
ISF	Islamic Social Finance
IFSB	Islamic Financial Services Board
IFSI	Islamic Financial Services Industry
IIFS	Institutions offering Islamic Financial Services
OJK	Otoritas Jasa Keuangan
REITs	Real Estate Investment Trusts
RSA	Regulatory and supervisory authority
SDG	Sustainable Development Goal
SEA	South-East Asia
SRI	Sustainable and Responsible Investment
WCP	<i>Waqf</i> Core Principles
ZCP	<i>Zakāh</i> Core Principles

## Section 1: Introduction

### 1.1. Background

**Islamic Social Finance (ISF) plays a crucial role in providing liquidity and funding support, especially to micro and small enterprises within the Islamic finance industry.** The significance of ISF in achieving the United Nations (UN) Sustainable Development Goals (SDGs) cannot be overemphasised, stemming from its proven ability to combat poverty and provide supplementary funding for economically vulnerable projects that might be overlooked by the private and public sectors.<sup>1</sup> Given its substantial impact on the economy, initiatives to mainstream ISF are gaining momentum among stakeholders and ISF has evolved beyond its traditional foundations, including *sadaqah*, *zakāh*, and *waqf*, to be integrated with more complex instruments such as *ṣukūk*. This expansion draws attention to the regulatory landscape, which currently exhibits gaps in both conventional and Islamic spaces. However, several issues hinder the potential contribution and regulation of ISF.

**The conceptualisation of ISF remains somewhat unclear and thus poses a challenge in formulating standardised regulations.** This is due to the diverse practices of its two essential components, namely Sharī'ah-compliant social solidarity instruments (*zakāh*, *sadaqah*, *waqf*, *qardḥasan*) and social finance institutions (Islamic microfinance,<sup>2</sup> Islamic foundations, charitable organisations/NGOs, etc.). This diversity poses a challenge in formulating standardised regulations.

**The hybrid nature of the ISF sector, which at times entails operating at the intersection of philanthropy and commerce, makes certain institutions susceptible to mission drift.** Sustainability exigencies amid unclear regulations portends a predisposition of the ISF institutions prioritising commercialisation over social welfare as their traditional role. This complexity further complicates the regulation of ISF institutions, as most jurisdictions lack dedicated ISF regulations, and these institutions may not fit neatly into existing regimes for charities, securities, or corporations. Consequently, regulators must ensure ISF institutions remain committed to their social missions.

**Although ideally premised on the theological communitarian philosophy of Islam, which underlies its inherent compassion and altruism, the growth of the ISF sector is far from its potential.** To achieve significant milestones, there is an urgent need for standardised regulatory practices to enhance efficiency and safeguard against potential integrity issues that could negatively impact social welfare. Additionally, concerns arise over the substantial unregulated and inefficient money flow through various ISF institutions in numerous jurisdictions.<sup>3</sup>

**The Islamic Financial Services Board (IFSB) recognises the importance of ISF, from both a financial stability consideration and the increasing linkages and dependence between the ISF and the three main IFSI segments: Islamic banking, Islamic capital**

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<sup>1</sup> IFSB Stability Report (2021)

<sup>2</sup> Defined as the confluence of Islamic financing principles and the concept of financial inclusion. Commonly used are cost-plus sales (*murabaha*), interest-free loans (*qardḥassan*), but also forward sales (*salam* and *istisn'a*) and leasing (*ijarah*).

<sup>3</sup> N. Kyriakos-Saad, M. Vasquez, C. E. Khoury and A. E. Murr (2016). "Islamic Finance and Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)", IMF Working Paper No. WP/16/42, Washington, D.C.: IMF.

markets (ICM), and *takāful*. In 2019, the IFSB issued a technical note focused on financial inclusion, *TN-3: Technical Note on Financial Inclusion and Islamic Finance*. TN-3 offers guidance and recommendations for effective regulation and supervision within the financial sector, with a specific focus on promoting financial inclusion through Islamic finance. This entails finding a balance between the benefits of regulation and supervision, considering proportionality, and being mindful of the potential risks and costs involved. TN-3 includes a chapter on ISF, which offers comprehensive regulatory and supervisory guidelines for regulatory and supervisory authorities (RSAs).<sup>4</sup>

## 1.2. Objectives and Scope

**The purpose of this paper is to analyse current regulatory and supervisory practices regarding ISF in various jurisdictions.** Noteworthy feedback from respondents is used to identify areas of consensus in ISF practices across jurisdictions to address existing gaps. The objective is to identify commonalities and differences and explore various aspects, including the incorporation of Shari'ah-compliant instruments, technological utilisation, and regulatory challenges.

**This working paper focuses on a comprehensive scope of ISF institutions.** This encompasses *zakāh*, *sadaqah*, Islamic microfinance, *waqf*, micro-*takāful*, Islamic cooperatives, and other institutions that specific jurisdictions may categorise under the domain of ISF. This categorisation aligns with the predefined parameters of the research. Additionally, the paper explores factors contributing to the growth of ISF institutions and examines obstacles encountered by supervisors. It offers recommendations to overcome challenges faced by regulatory and supervisory authorities, aiming to improve existing practices related to ISF. The findings are envisaged to inform the future work of the IFSB in related areas.

## 1.3. Methodology

**This paper examines regulations, relevant documents, and survey responses to analyse and compare the regulatory and supervisory practices of ISF across jurisdictions.** The study also considers the role of ISF in promoting order and safeguarding the interests of beneficiaries. The survey was circulated to IFSB's RSA member organisations, with responses received from 19 organisations across 13 countries where Islamic finance is practiced. The questionnaire included closed-ended and open-ended inquiries, providing insights specific to each jurisdiction. It is assumed that the responses accurately reflect the state of ISF in their respective areas, as they were completed by the relevant authorities responsible for ISF. In addition, the paper also benefited from insights provided by industry experts and thought leaders during the inaugural IFSB Consultative Group (ICG). The ICG was held alongside the IFSB Annual meetings in August 2023 in Riyadh, Saudi Arabia. The revised draft was circulated to the IFSB RSA members for consultation as part of the publication due process. The valuable feedback obtained provided a basis for another round of specific consultation with some IFSB RSA members via arranged interview sessions to provide richer insights and clarity on some notable developments indicated in their earlier written responses.

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<sup>4</sup> IFSB TN-3 (2019)

## 1.4. The Structure

**The working paper is divided into four distinct sections, each contributing to a comprehensive but integrated analysis.** Subsequent chapters incorporate a thorough examination of the collected survey data and relevant literature. Section 2 critically reviews regulatory frameworks, shedding light on the range of operational institutions found in various jurisdictions, responsibilities assigned to regulators, and the factors that drive regulatory measures. Section 3 delves into the supervisory frameworks for ISF, exploring the risk factors associated with ISF institutions, identifying barriers to effective supervision, and addressing existing gaps in the regulatory landscape. Finally, Section 4 concludes by synthesising the findings and drawing valuable lessons for policymakers, accompanied by a set of recommendations.

## Section 2: Regulatory Framework

### 2.1. Operating Institutions

ISF encompasses the provision of financial resources to support vulnerable individuals in the society who often face difficulties in accessing traditional financial services. Nonetheless, compared to other sectors of Islamic finance, such as Islamic banking, Islamic capital markets, and *takāful*, ISF is considered to be the least regulated. This sector faces several challenges, including regulatory responsibility falling on various agencies within a jurisdiction. Additionally, RSAs from different jurisdictions have focused their efforts on developing Islamic social finance as a tool to improve financial inclusion before proposing regulatory frameworks, perhaps due to the fact that Islamic social finance is not considered to significantly impact the safety, soundness, and stability of the financial system, which is the primary concern of regulators.

Currently, there is no universally accepted definition of what constitutes ISF instruments. While there is a consensus that traditional instruments like *waqf*, *sadaqah*, and *zakāh* fall within the scope of ISF, there are differing opinions regarding instruments such as Islamic microfinance, Islamic cooperatives,<sup>5</sup> and micro-*takāful*.<sup>6</sup> For example, some definitions of ISF include *infaq* while excluding Islamic cooperatives and micro-*takāful*, while others incorporate instruments like *qard* and *kafālah*.

Figure 1: Definition of ISF by different institutions

No	Institution	Components of ISF							
		<i>Zakāh</i>	<i>Waqf</i>	<i>Sadaqah</i>	Micro-finance	Foundations/NGOs	<i>Kafālah</i>	<i>Qard</i>	<i>Takāful</i>
1	IFSB	✓	✓	✓		✓		✓	
2	Islamic Research and Training Institute	✓	✓	✓	✓		✓	✓	
3	Islamic Relief	✓	✓	✓	✓			✓	✓
4	United Nations	✓	✓	✓	✓			✓	

The survey conducted among member countries yielded diverse outcomes, particularly regarding the recognition of formal ISF institutions and the presence of regulations governing them. The responses varied, highlighting the absence of standardised practices, with different countries exhibiting distinct approaches and types of existing regulations. The findings emphasise the need for greater harmonisation and consensus-building within the field of ISF, as the lack of uniformity across practices and regulations may present challenges.

Generally, the results highlight that while there are institutions for a varying range of ISF practices within surveyed jurisdictions, only a limited number of countries consider these institutions to be formally offering ISF services. An exception to this is Indonesia,

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<sup>5</sup> An Islamic cooperative conducts activities and businesses based on Shari'ah principles. Being a non-banking financial institution, its main objective is to enhance the social and economic welfare of its members.

<sup>6</sup> Micro-*takāful* is widely known in the industry as *takāful* for low-income populations. In general, *takāful* terms, "low-income" means that section of the population that is customarily not eligible and not invited to participate in any of the *takāful* plans of any *takāful* operator (TO).

where all the identified categories of ISF institutions are present and even considered to be rendering services formally. The country also includes crowdfunding as another form of ISF. Recently, the platform Fundex was created to carry out ISF activities through the WAKAFESTASI program.<sup>7</sup>

**For traditional types of ISF, the results reveal that while most responding jurisdictions have *waqf* and *zakāh* institutions, only a few have *sadaqah* institutions.** *Zakāh* and *waqf* are predominantly recognised as formal institutions engaging in ISF activities, whereas *sadaqah* is the least recognised. For instance, in Libya, where *waqf* and *zakāh* are formally recognised, the absence of institutions offering these services may be attributed to informal practices rather than a complete lack of them.

**As for more contemporary forms of ISF, such as Islamic microfinance, micro-*takāful*, and Islamic cooperatives, the findings indicate that most jurisdictions have institutions offering Islamic microfinance, surpassing the number of jurisdictions with some form of traditional ISF.** This dominance holds true across jurisdictions where Islamic microfinance is formally considered part of ISF. On the other hand, institutions offering Islamic cooperatives are present in only a few jurisdictions, and even fewer countries formally recognise them as rendering ISF services, suggesting a possible absence of formal regulations for Islamic cooperatives. Micro-*takāful*, among all the listed forms of ISF, has a more extensive list of available institutions across jurisdictions and is more likely to be considered to be formally offering ISF compared to Islamic cooperatives.

**Furthermore, observations in Southeast Asian jurisdictions reveal distinctive characteristics regarding ISF.** In Malaysia, the definition of ISF does not include for-profit institutions like micro-*takāful* and Islamic microfinance unless they involve the intermediation of philanthropic capital. This means that these institutions are considered part of ISF only when they facilitate the utilisation of philanthropic funds. In Indonesia, ISF practices extend to Islamic banks, who are allowed to carry out social functions in the form of *baitulmal* institutions. Additionally, both Indonesia and Malaysia acknowledge the inclusion of digital platforms as components of ISF. They specifically recognise digital platforms utilised for crowdfunding-based donations as part of ISF.

**These variations in the definitions of ISF across jurisdictions have significant implications for the regulatory landscape and the responsible regulatory bodies.** It is evident that different countries categorise and acknowledge different instruments and institutions within the realm of ISF. This underscores the importance of establishing clear regulatory frameworks that align with the specific understanding and practices of ISF across jurisdictions.

## 2.2. Regulatory Practices and Responsibilities

### 2.2.1. Regulatory Authorities

**Due to the enduring interest in the UN SDGs and the increasing focus on Environmental, Social, and Governance (ESG) factors, it is not surprising to witness a**

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<sup>7</sup><https://fundex.id/wakafestasi#:~:text=Wakafestasi%20merupakan%20pengembangan%20dari%20konsep,manfaat%20yang%20berkelanjutan%20untuk%20umat>.

**global rise in the social finance sector.** This surge in interest is accompanied by a substantial influx of funding, primarily from the private sector. ISF follows a similar trend, with annual *zakāh* funding estimated to range between \$200 billion to \$1 trillion.<sup>8</sup> Given this growing momentum, it is essential to address the regulatory aspect of ISF. As mentioned earlier, one of the key weaknesses in the sector is the lack of regulation and of standardised regulations across jurisdictions. The wide diversity in definitions and practices emphasises the need for regulatory frameworks that can effectively govern these multifaceted activities. Therefore, it is crucial to identify the regulatory bodies responsible for overseeing and supervising ISF institutions within their respective jurisdictions.

**When examining the regulatory landscape of ISF institutions, it becomes evident that there are significant variations among the surveyed jurisdictions in terms of the responsible governing bodies.** In most jurisdictions, the primary statutory authority for governing ISF activities lies with the government ministry, department, or agencies. Additionally, many jurisdictions mention the involvement of the central bank and securities commission either as the primary responsible entities or as part of the regulatory and supervisory framework for these institutions.

**In jurisdictions that regulate Islamic microfinance, the central bank is typically designated as the statutory regulatory body. However, there are exceptions to this pattern, as observed in the cases of the Philippines and Bangladesh.** In the Philippines, the statutory regulatory bodies that are responsible for regulating and supervising Islamic Social Finance are the central bank, Bangko Sentral ng Pilipinas (BSP), as well as the Securities and Exchange Commission (SEC). The BSP exercises regulatory powers and supervision over all types of banks operating in the Philippines, including microfinance-oriented banks that are established either as a thrift bank or rural bank and Islamic Banks and Islamic Banking Units that may offer Islamic microfinance products and services. Among the functions of the SEC is the establishment of the Microfinance NGO Regulatory Council (MNRC). On the other hand, Bangladesh, which is recognised as a key jurisdiction in microfinance, has an independent regulatory body known as the Microcredit Regulatory Authority (MRA) responsible for supervising and regulating Islamic microfinance institutions. A similar scenario can be seen in the way *zakāh* and *waqf* are managed in countries like Indonesia, where the government established both the National Amil *Zakāh* Agency (BAZNAS) and the Indonesian *Waqf* Agency (BWI) as authorised institutions for *zakāh* and *waqf* respectively.

**Across jurisdictions, it is common to find multiple regulatory bodies overseeing the operations of ISF,** which is understandable given the distinct characteristics of different ISF institutions. For example, Islamic microfinance institutions, which function as deposit-taking entities, require different regulatory bodies compared to traditional ISF institutions that rely on donations and philanthropy.

- **In Libya and Kenya,** where *waqf* and *sadaqah* are formally recognised as ISF institutions, the central bank assumes the role of the statutory regulator. In contrast, some other jurisdictions have entrusted the responsibility of regulating traditional forms of ISF to government ministries and religious councils.

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<sup>8</sup> <https://islamic-relief.org/islamic-social-finance/>

- **In the Maldives**, the Maldives Inland Revenue Authority plays a significant role as a statutory authority overseeing ISF operations.
- **In Saudi Arabia**, it is only when a social venture makes a profit that the central bank intervenes and applies the prudential rules that social enterprise must comply with. This approach, treating social impact as an economic model instead of as Islamic social finance, allows regulators to consider ISF institutions as creators of shared value. In this way, regulation becomes less of an issue since it is the regulation of a business.
- **In Malaysia**, the regulation of ISF falls within the purview of various institutions; Bank Negara Malaysia (BNM) specifically regulates business and financial intermediation activities conducted by financial institutions, and this may include ISF-related activities. BNM does not issue separate regulations for financial institutions that offer social finance offerings. However, there are ongoing efforts to integrate social finance with the financial intermediation activities of financial institutions. Such integration is currently undertaken as a developmental initiative and part of BNM's financial inclusion agenda. For example, iTEKAD, is an initiative supported by BNM with the aim of enabling low-income microentrepreneurs to generate stable long-term income. Each bank implements its own iTEKAD program which include three key elements, namely seed capital, structured training, and microfinance. The seed capital provided is financed by the contribution of social finance funds from various implementing partners to iTEKAD programs, including *zakat*, cash *waqf*, public donations, etc.

**This diversity observed across jurisdictions reflects the unique nature of ISF activities and the different types of institutions involved.** Understanding these variations in definitions and regulatory landscapes is crucial for policymakers and regulators to develop targeted and appropriate regulations that align with the specific operations of ISF in their respective jurisdictions. With the rapid growth and the significant amount of money flowing through ISF channels, it is crucial for regulators to remain vigilant and create adequate tools to mitigate the potential for fraud. The survey responses indicate that the prevalent regulatory practice involves multiple authorities governing this sector, raising interest in identifying the regulatory practice when addressing fraud.

**To gain deeper insights into industry practices, respondents were asked whether it would be permissible for other RSAs to intervene if an ISF institution's activities are considered fraudulent or stray beyond their existing regulatory scope.** A majority of the responses noted that even if it falls outside their purview, RSAs can take action if ISF activities are considered fraudulent. In jurisdictions like Kenya, if an Islamic microfinance institution engages in fraudulent activity, the Capital Markets Authority (CMA), which is the regulatory authority for Islamic capital market institutions in Kenya, may take regulatory action against the institution. Similarly, in Pakistan, where some aspects of ISF, especially the traditional forms, are supervised at the government level under government ministries and agencies, the Securities and Exchange Commission (SECP) can initiate enforcement proceedings if institutions are found to be engaged in deceptive practices or carrying out unauthorised roles. It is important to note that the specific regulatory bodies involved in addressing fraud may vary across jurisdictions. In some cases, it may be the central bank, while in others, it could be the monetary authority or the securities commission, depending on the regulatory framework in each jurisdiction.

### 2.2.2. Supplementary Frameworks

**The importance of supplementary frameworks becomes more apparent as traditional tools of *zakāh*, *waqf*, and *sadaqah* are adapted into contemporary financial structures and instruments to increase outreach and financial inclusion.** To fully harness this potential, supportive policies are necessary to facilitate the efficient mobilisation, utilisation, and management of ISF resources, as well as their integration with other forms of finance to enhance inclusivity and affordability. These policies should address both the micro and macro levels. At the macro level, there is a need for policies that establish enabling legal, regulatory, and fiscal frameworks and provide the necessary supporting infrastructure. Similarly, at the micro level, policies need to prioritise measures that enhance institutional accountability and transparency, improve governance practices, diversify product offerings, and empower economically disadvantaged individuals through initiatives promoting financial literacy and responsibility.

**The survey indicates that while most jurisdictions have some complementary regulatory frameworks available, fewer utilise them to complement ISF activities.** This trend persists for all the mentioned frameworks. For instance, while several countries have an Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework available, only half of the respondent RSAs highlighted its use to complement ISF activities. Similarly, while most respondents noted the framework for use by collection intermediaries or agents, only one-fifth reported its utilisation to complement ISF activities. This indicates a gap, where these frameworks are present but are less commonly used to complement ISF activities. In the case of the Philippines, BSP adopts a single regulatory and supervisory framework. Hence, existing frameworks covering transparency, disclosure, and data protection as well as AML/CFT are applied to all types of BSP-supervised financial institutions. In Indonesia, where OJK has published specific transparency and disclosure frameworks related to the disclosure of ISF (*zakāh*, *infaq*, *sadaqah*, *waqf*, and other social funds) received and distributed by banks to the social institutions. In Pakistan, although ISF institutions are present, complementary frameworks are not applied to the activities of ISF.

**In terms of industry-level guides, some jurisdictions have undertaken initiatives to issue benchmark guidelines, frameworks, and other documents to support the growth and harmonisation of ISF practices.** Bank Indonesia, in collaboration with IRTI-IsDB, *Zakāh* National Board (BAZNAS), and *Waqf* National Board (BWI), has issued the *Zakāh* Core Principles (ZCP) and *Waqf* Core Principles (WCP), that serve as a benchmark for activities related to *zakāh* and *waqf*. The Securities Commission of Malaysia will publish the 2<sup>nd</sup> edition of *Waqf* Assets Book<sup>9</sup> as a part of a national *Waqf* Masterplan to develop idle *waqf* assets. Moreover, it was found that many of the surveyed jurisdictions have established frameworks for transparency and disclosure, which play a crucial role in ensuring transparency and building public trust within the ISF sector. These frameworks serve as valuable tools to enhance accountability and promote confidence in the operations of ISF institutions. However, it is worth noting that despite the significant involvement of ISF institutions as agents or intermediaries, the availability of a specific framework for the use of collection intermediaries or agents is quite limited across jurisdictions. This finding aligns with the earlier discovery of a general absence of formal regulation for the ISF sector. Nevertheless, the importance of

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<sup>9</sup> Securities Commission Malaysia (2014)

addressing this gap should be recognised, as implementing a comprehensive framework in this area would contribute to better governance and oversight within the ISF sector.

### 2.3. Current Regulatory Regimes and Change Process

**ISF is a unique and multifaceted sector that combines both finance and philanthropy, but presents a unique challenge known as mission drift**, wherein the original objectives of ISF may be diluted or compromised in pursuit of financial sustainability, increased profit, or growth. The hybrid nature of ISF arises from the fusion of financial objectives with social welfare goals, giving rise to innovative financial instruments aimed at promoting social and economic development. Understanding the complexities of this hybrid nature and its potential impact on mission drift is vital to ensure the integrity and effectiveness of ISF in achieving its core objectives.

**Moreover, the hybrid nature of these institutions has significant implications for regulators and supervisors.** Due to their unique characteristics, conventional regulations that govern philanthropic or commercial institutions may not fully apply to them. To effectively address and limit the occurrence of mission drift, regulators and supervisors must demonstrate diligence and attentiveness in bridging the regulatory gap. This may involve continuous consideration and thorough review of existing regulations to identify any gaps that need filling. When asked about the regulatory regime in their jurisdictions, it becomes evident that for most ISF activities across various jurisdictions, there is an ongoing effort to amend existing regulations to include ISF activities, rather than applying established regulations. This indicates a prevailing desire to advance the sector and create favourable environments to ensure its continuous growth, despite its relative infancy across jurisdictions. Interestingly, fewer countries reported leaving the sector unregulated.

**Regarding specific ISF activities across jurisdictions, Islamic microfinance appears to be the most well-regulated in terms of existing regulations.** This is consistent with the understanding that Islamic microfinance is the most formally recognised ISF activity, and in most of the jurisdictions surveyed, Islamic microfinance services are offered by financial institutions regulated by local regulatory authorities and RSAs rather than by religious organisations. With respect to other forms of ISF, a greater number of surveyed jurisdictions have specific regulations for *waqf* operations compared to other ISF activities such as cooperatives, micro-*takāful*, and *sadaqah* which have fewer tailored regulations. *Zakāh* appears to be the least regulated among RSAs that responded. However, no RSAs reported unregulated micro-*takāful* and cooperatives, which might not necessarily indicate their advanced state of regulation but rather the lesser prevalence of the activity in the jurisdictions.

**Similarly, efforts to amend existing regulations for ISF activities are more concentrated in Islamic microfinance, followed by *waqf* and micro-*takāful*.** The survey indicates a lesser emphasis on efforts to enhance existing regulations for *zakāh*, *sadaqah*, and Islamic cooperatives. This indicates that while many countries strive to regulate the ISF sector more effectively, Islamic microfinance receives greater attention than other ISF activities. In certain jurisdictions, the existing regulations for ISF are not formulated at the central level but rather developed by local experts and adopted as industry practices within the ISF sector. This decentralised approach to regulation underscores the need for further standardisation and central guidance to ensure consistency and effectiveness across jurisdictions.

**Most respondents were of the view that existing regulations applied to ISF in their jurisdictions are sufficiently prescriptive, encompassing both permitted and restricted ISF activities.** On the other hand, those who perceived the existing regulations as less prescriptive cited concerns about their limitations. In some jurisdictions, regulations only apply to specific ISF products and not to the institutions themselves. In Indonesia, while there are existing regulations, there is also a recognition of other aspects that need to be looked at, such as aspects of risk management for *amil* and *nazir*, standards for the level of the financial soundness of *amil* and *nazir*, and regulations related to the digitisation of *zakāh* and *waqf* management. Additionally, in some jurisdictions, there are limitations in terms of the absence of dedicated regulations that are specifically tailored to ISF, as existing regulations may encompass both conventional and Islamic institutions, potentially overlooking the unique challenges and considerations of Islamic principles. In the Maldives, efforts are underway by relevant authorities to develop specific regulatory frameworks for *zakāh* and *waqf*, but these initiatives are acknowledged to require time before effective implementation.

**Most respondent RSAs reported that dedicated regulations for ISF do not impose more obligations or greater regulatory burden than pre-existing regulations.** This suggests that creating regulations allows jurisdictions to eliminate redundant or inapplicable aspects of existing regulations, making compliance relatively straightforward for ISF stakeholders. For instance, Jordan issued specific instructions for anti-money laundering (AML) and terrorist finance for microfinance companies, establishing adequate controls to prevent the misuse of microfinance companies for illegal activities while aligning with the specific requirements and considerations of ISF activities. Indonesia has issued several dedicated regulations for the supervision of ISF such as those related to Shari'ah-compliant audit regulations, regulations on accreditation assessment standards for *amil zakāh* institutions, and regulations on aspects of *waqf* supervision, especially cash *waqf* innovations. Additionally, there are two transformative initiatives driving the evolution of Islamic social finance in Indonesia. The first initiative is the enactment of the new "Law on Financial Sector Development and Strengthening", which allows Islamic banks to assume the role of *nazir*. Under this new mandate, Islamic banks can channel *waqf* funds towards *waqf* projects, necessitating revisions to the current *waqf* law and related regulations. The second noteworthy initiative is the implementation of a digitised Islamic social finance management system, offering an additional avenue for mobilising funds. This digital approach is aimed at contributing substantially to economic development programs, particularly those focused on poverty alleviation and holistic human development. Similarly, in Saudi Arabia there are regulations aimed at safeguarding the legitimate intent of providing humanitarian assistance abroad through charitable donations originating from the Kingdom. Consequently, any charitable donations intended for international purposes will require approval from the Foreign Ministry, provided that certain rigorous reporting and accounting requirements are met.<sup>10</sup>

**The surveyed jurisdictions highlighted a combination of factors triggering changes or reviews in the ISF regulatory framework, but they varied among jurisdictions.** The responses indicate that the most common trigger for regulatory reviews was an outcome of consultation with firms, industry bodies, religious organisations, academia, donors, and other stakeholders. Respondents also mentioned triggers such as analysing regulatory frameworks

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<sup>10</sup> Al Mamun, M.S., Adewale, A.A., Abu Mwis, G., Youssef, N. (2019). "Joint IFSB-AMF Working Paper on Money Laundering and Financing of Terrorism (ML/FT) Risks in Islamic Banking", *IFSB Working paper Series WP-12/12/2019*. <https://ifsb.org/download.php?id=5509&lang=English&pg=/sec03.php>

of other jurisdictions, observing new technological and innovative developments in a regulatory sandbox environment, and utilising supervisory powers and external evidence for diagnostic or thematic reviews of existing ISF regulations. For example, Kenya noted that the regulatory framework was reviewed to align with international standards and best practices in Islamic finance. In Indonesia, the driving factors also included public demand from *nazirs* requesting more professionalism and transparency to boost public trust. A few jurisdictions indicated that feedback obtained from publications following a call for evidence or consultation papers triggered reviews to the regulatory framework for ISF.

## 2.4. Drivers for Regulatory Development in ISF Institutions

**The sustainability of ISF and the increasing drive for greater integration have highlighted the issue of inadequate regulations.** Unsupported policies and regulations can hinder the sector's sustainability, while the presence of different governing bodies for individual ISF institutions within jurisdictions poses a threat to integration. Therefore, regulatory bodies must revise laws to accommodate the continuous growth of the sector and ensure that the regulatory framework aligns with the evolving needs and challenges of ISF.

**While understanding the pattern and timing of regulatory change is important, it is equally important to understand how and why these changes occur.** Member RSAs were asked about the main drivers for regulatory development within their jurisdictions. Responses indicate that jurisdictions were motivated by various factors, with a majority being driven by government policies or strategies for socioeconomic development. Other significant factors were approaches from other jurisdictions, industry-driven requests for regulation or guidance, and the increasing prominence and size of the ISF sector. Some jurisdictions were motivated by the need to mitigate the risks of money laundering and financing of terrorism in ISF institutions, as well as the risk of mission drift. However, only a few institutions mentioned being influenced by new emerging evidence from supervisory work.

**When asked if there were considerations for reviewing or changing ISF regulations in their jurisdictions, respondent RSAs were evenly divided.** Among those affirming, changes were expected to occur within a year or within the next 4-5 years, with only a few countries anticipating changes within 2-3 years. Several RSAs also outlined structural changes they expect to implement in the field of ISF in their respective jurisdictions.

- **Pakistan** aims to formalise ISF by connecting *waqf* funds with collective investment vehicles, facilitating Islamic crowdfunding for ISF, and issuing guidelines to enhance disclosures for companies operating under charitable licenses.
- **Malaysia** has made additional amendments to enable the issuance of real estate investment trusts (REITs) and exchange-traded funds (ETFs) with *waqf* features.
- In **Indonesia**, the two initiatives mentioned previously the “New Law on Financial Sector Development” and “Strengthening and Implementation of a Digitalised ISF Management”, necessitate amendments to the current *waqf* law and other related regulations. Future regulations would also include requirements for *nazir* competency certification, obligatory report preparation, connectivity to an e-reporting system/platform, and the integration of digital innovation into the entire process, starting from *waqf* pledges, payments, and the distribution of benefits to beneficiaries.

- In **Oman**, the focus is on integrating ISF into commercial finance by enabling *waqf* deposits and supporting *waqf* development through Islamic banks. Future regulations in Oman will primarily concentrate on the role of Islamic banking entities (full-fledged Islamic banks and Islamic windows) in supporting ISF. This approach is similar to Malaysia's efforts to integrate ISF into commercial Islamic finance.
- **Some other jurisdictions** like Sudan adopt a more laissez-faire approach, making amendments to laws based on evolving industry changes. This approach aims to maintain flexibility to accommodate developments in ISF without imposing strict regulations.

Overall, these examples highlight the diverse approaches and expectations of different jurisdictions regarding changes in ISF regulations, with some countries emphasising structural reforms to enhance the integration and effectiveness of ISF within their financial systems.

## 2.5. Risk Factors for ISF Institutions

**Innovation continues to shape the ISF sector. However, RSAs also need to be mindful of how these innovations align with regulatory objectives**, such as financial stability, integrity, and risk mitigation, as well as ensuring consumer protection, the latter being a fundamental aspect of the financial inclusion that ISF institutions aim to achieve. IFSB standards and other guidance on risks specific to the Islamic financial sector<sup>11</sup> may also be applicable to ISF institutions with certain considerations of proportionality, although they do not address the specific issues pertinent to the ISF sector.

**Given the increasing utilisation of technology in providing ISF, technology and cyber risks are prominent considerations.** Technology failures and vulnerability to cyberattacks should be considered in risk management frameworks for ISF. However, while important, these risks may not be specific to ISF.

**Another risk that is relevant to ISF is mission drift, which refers to the risk of ISF institutions deviating from their intended purpose of poverty alleviation and shifting focus towards financial gains.** While this risk is indicated as being important, only a few RSAs indicated that institutions offering ISF in their jurisdiction were susceptible to mission drift.

**Most respondents highlighted the heightened susceptibility of ISF institutions to risks associated with anti-money laundering and combating the financing of terrorism (AML/CFT).** Improper mobilisation and disbursement of funds within ISF institutions can expose them to AML/CFT risks, making it essential for RSAs to implement robust measures and regulatory frameworks to ensure compliance with international standards and recommendations of the Financial Action Task Force (FATF).

**Legal uncertainties can also pose risks to ISF institutions.** Having clarity in legal provisions governing financial institutions is vital to prevent regulatory abuse and establish a solid foundation for the effective operation of ISF institutions. However, only a few jurisdictions

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11 IFSB-1, IFSB-12, IFSB-14, GN-2, and GN-6

reported a high susceptibility of ISF institutions to legal uncertainties, suggesting that this risk may not be widely perceived in most member jurisdictions.

**ISF can also be susceptible to reputational risk**, and failure to effectively detect and mitigate such risks can severely damage public trust and confidence, which can be detrimental to the institutions. In the case of ISF institutions, a lack of confidence and trust in their reputation and integrity can have a particularly negative impact on stakeholders, such as donors. Donors contribute to these institutions based on their reputation as Sharī'ah-compliant entities, especially in the case of *zakāh*, *waqf*, and *sadaqah*, which rely on public donations. In countries without standardised procedures for collecting and disbursing these funds, donors have discretion to choose which ISF institution they support. Negative information about a particular institution may harm donation levels. Therefore, it is not surprising that a significant number of RSAs responded that ISF institutions in their jurisdictions are highly susceptible to reputational risk. Moreover, the inability of institutions to effectively detect and mitigate reputational risk can also undermine their sustainability. A reputational hazard for an ISF institution could result in a sudden decrease or cessation of funding from donors.

**Surveyed jurisdictions also acknowledged that institutions offering ISF are highly susceptible to sustainability risk.** This highlights the importance for both RSAs and institutions to be aware of and properly mitigate such risks. Indonesia noted the current supervision and guidance carried out by the Ministry of Religion of ISF institutions to ensure the minimisation or reduction of such risk.

**The majority of jurisdictions indicated susceptibility to at least three of the mentioned risks, while also highlighting several other specific risks.** For example, the Philippines identified the potential risk of Sharī'ah non-compliance, citing a lack of sufficient Sharī'ah experts who can provide proper guidance to ISF institutions. Shariah non-compliance risk is also closely linked to reputational risk, underscoring the importance of ensuring adherence to Islamic principles in the operations of ISF. Malaysia specified risks related to compliance, including non-compliance with the regulatory framework and requirements, as well as financial risks arising from the valuation of ISF assets and cash flow management, highlighting the need for robust governance and compliance measures within ISF institutions. Lastly, Bahrain emphasised the potential credit risk faced by Islamic microfinance institutions, indicating the importance of assessing the creditworthiness of borrowers and managing potential defaults.

**The IFSB has issued relevant documents that touch on some of these issues**, however, they are based on the specificities of mainstream Islamic financial institutions. As a result, the peculiarities and unique risks within the ISF sectors have yet to be critically addressed.

## 2.6. Specific Disclosures for ISF Institutions

**The IFSB has issued a number of standards to enhance transparency and disclosure for Islamic capital markets, Islamic banks, and *takāful* segments.**<sup>12</sup> However, it is also important to look at disclosures that need to be specifically tailored for ISF institutions. These tailored disclosures provide a narrower perspective, ensuring the inclusion of streamlined requirements that may otherwise be overlooked.

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<sup>12</sup> IFSB-19, IFSB-22, IFSB-24 and IFSB-25

**The majority of respondents acknowledged the presence of specific disclosure requirements for ISF institutions.** However, the details of these requirements vary across jurisdictions. In Kenya, ISF institutions are expected to disclose information related to Shari'ah governance, such as the names of supervisory board members, Shari'ah compliance details, and the percentage of Shari'ah-compliant and non-compliant assets. Additional information may include *zakāh* collection and distribution, overall governance structure, profit and loss sharing arrangements, and investment policies.

**A common disclosure requirement across jurisdictions relates to the policies for fund distribution and collection, as well as disclosure of product structure.** Some jurisdictions also require disclosure of information on the sources and uses of charity in banking institutions, disclosure of material changes, and the provision of periodic reports, annual reports, internal audit reports, and information on the recipients/beneficiaries of funds.

**Most jurisdictions noted that other organisations and institutions within their jurisdiction, such as accounting and auditing regulators, do not specifically require ISF-related disclosures.** Among the few jurisdictions that do have such requirements, Pakistan indicated the presence of accounting standards for not-for-profit organisations (NPOs) and an exposure draft of accounting standards on financial statement disclosures for *zakāh* received by an entity. Indonesia indicated the issuance of accounting standards for *zakāh*, *waqf*, and charity.

**ISF tools applied in the capital markets or the banking sector entail specific disclosure requirements.** This includes disclosure requirements in Malaysia for Islamic collective investment schemes with *waqf* features and Sustainable and Responsible Investment (SRI) *sukūk* (under this purview, the RSAs include *waqf* projects as a part of SRI *sukūk*). In Indonesia, Islamic banks are mandated to publish the statement of sources and distribution of *zakāh* and *waqf* funds and a statement of sources and uses of *qarḍ hasan* funds. For *zakāh*, there is a financial audit obligation through a public accountant, while for *waqf* regulation, there is an option for disclosing the collection of cash *waqf* through a public accountant.

**Finally, among the RSAs that provided responses, the disclosure requirements for ISF activities vary depending on whether an institution is domiciled within its jurisdiction.** However, Malaysia and Kenya are among the few jurisdictions that indicated having consistent disclosure requirements for ISF activities regardless of the institution's domicile.

## **2.7. The Presence of Evaluation Criteria for ISF Institutions**

**Assessing the compliance and impact of ISF institutions within a jurisdiction is crucial for establishing an effective ISF ecosystem and for understanding their influence on potential beneficiaries.** Regulators' assessment of the impact of ISF institutions can help prevent mission drift and ensure that institutions remain aligned with their intended purpose. However, the survey revealed that the majority of RSAs across member jurisdictions do not assess the impact of ISF institutions operating within their jurisdictions. As noted by the Philippines, this could be attributed to the absence of institutions offering ISF in their jurisdiction.

**Among the RSAs that do assess the impact of ISF institutions, most indicated multiple mediums of assessment.** A majority of RSAs assess the impact of ISF institutions under

their purview through supervisory powers and external evidence to carry out a diagnostic or thematic review of the extent of ISF regulations. Additionally, many RSAs utilise procedures such as periodic peer reviews benchmarked against the performance of ISF institutions in previous years, as well as informal consultations with firms, industry bodies, religious organisations, academia, donors, and other stakeholders. They also consider the observation of new technological and innovative developments, including in a “test-and-learn” or regulatory sandbox environment as well as relevant feedback obtained from publications following a call for evidence or consultation paper. Only one jurisdiction reported conducting assessments via the periodic peer-review benchmarked against performances of ISF in the other comparable jurisdiction.

**Some jurisdictions employ unique methods tailored to their environment.** For example, Bahrain conducts assessments of ISF institutions through normal supervisory reviews, including prudential meetings, financial statement reviews, and inspections. In Malaysia, the Securities Commission undertakes thematic assessments of ISF as part of its developmental work. Overall, the assessment of compliance and impact plays a crucial role in ensuring the effectiveness, alignment, and positive outcomes of ISF institutions, and RSAs have a significant role to play in this process.

## Section 3: Supervisory Framework

**The presence of supervisory resources and bodies plays a crucial role in ensuring the smooth operations of institutions and establishing an effective framework for supervision.** It emphasises the need for robust systems to enforce supervisory tools and policies, aiming to prevent fraudulent practices. In a rapidly evolving financial industry, the importance of supervisory controls and resources is increasingly recognised by regulators. This applies to institutions offering ISF services as well. Considering the significant amounts of money involved in donations and deposits, discussions about implementing supervisory controls within the sector are well-founded.

### 3.1. Barriers to the Effective Supervision of ISF Institutions

**Recognising the importance of a comprehensive supervisory framework for effective oversight of ISF institutions, it is crucial to identify the barriers that exist in the supervision of these institutions.** Surveyed jurisdictions highlighted a number of obstacles to effective supervision of ISF.

**The most prevalent barrier to the supervision of ISF institutions highlighted by the survey is the limited expertise and human resources, both in terms of technical knowledge and technological capabilities, available for effective ISF supervision.** Additionally, a significant number of RSAs face obstacles related to regulatory fragmentation and a lack of coordination among multiple regulators. Other challenges include limitations in obtaining requisite data on the volume of economic activities and the number of ISF institutions, as well as legal uncertainties arising from frameworks that intersect with the purview of other regulators, such as data protection. An example of regulatory fragmentation which may inhibit coordination among regulators is highlighted by Malaysia, where legislation places Islamic affairs, including *zakāh* and *waqf*, under the purview of the State legislature, administered by respective State Islamic Religious Councils. However, elements of ISF, such as *waqf*, also exist in the capital market, which falls under the jurisdiction of the Securities Commission. A few jurisdictions also highlighted barriers related to a large number of ISF institutions operating informally outside the formal supervisory perimeter and the rapid pace of technological advancements and their deployment in ISF activities. Lastly, some jurisdictions also mentioned limited funding availability dedicated to the supervision of the ISF sector as an obstacle.

#### Barriers and challenges to effective supervision of ISF

- limited expertise and human resources
- regulatory fragmentation
- lack of coordination among multiple regulators
- legal uncertainties
- ISF institutions operating informally outside the formal supervisory perimeter
- rapid pace of technological advancements
- limited funding availability and resources dedicated to supervision of the ISF sector

### 3.2. Gaps in the Supervisory and Regulatory Provisions for ISF Institutions

The identification of barriers to effective supervision of ISF institutions also helps uncover existing gaps in current supervisory and regulatory practices. This understanding allows for the implementation of targeted actions and initiatives to address these gaps. Responses from RSAs in member jurisdictions highlighted various areas where guidance is needed from standard setters such as the IFSB regarding the gaps in regulation and supervision of ISF institutions and their activities. The specific areas requiring guidance vary across jurisdictions.

#### Identified gaps in supervisory and regulatory provisions for ISF institutions by respondents:

- need for standardised reporting and monitoring of ISF-related activities
- need for additional guidance on risk and liquidity management for ISF institutions
- need for more guidance on stronger governance of ISF institutions
- harmonising guidelines for supervision of micro-*takāful* and Islamic cooperative institutions

Recognising the importance of effective supervision in ensuring the compliance of ISF institutions with Sharī'ah principles, some jurisdictions express the need for a comprehensive review and assessment of the regulatory and supervisory measures in place. Additionally, some surveyed jurisdictions highlighted the need for best practices in supervising ISF institutions, including guidance on updating regulations to adapt to evolving technologies, emerging issues, and digital platforms for *zakāh* and *waqf* collection. Furthermore, as certain jurisdictions actively expand the scope of ISF, e.g., Pakistan plans to link *waqf* funds with collective investment vehicles to facilitate Sharī'ah-compliant microlending through Islamic crowdfunding, they seek consultation with the IFSB for guidance and direction in supervising these institutions and coordinating with central banks and government agencies. This guidance would be particularly beneficial in jurisdictions where ISF oversight falls under multiple agencies and ministries, as it would facilitate coordination among them. These suggestions from RSAs aim to enhance the supervisory capabilities of ISF institutions, especially in jurisdictions that currently lack comprehensive frameworks.

## Section 4: Conclusion And Recommendation

**This paper gathers responses to facilitate a comprehensive discussion and comparative analysis of various practices of ISF regulation across different jurisdictions and identify potential regulatory gaps.** It identifies both commonalities and distinctions, in terms of regulatory and supervisory practices governing ISF. The results provided valuable insights that shed light on the realities of ISF.

**Discussions and responses from member jurisdictions highlighted several important factors related to the supervision and regulation of ISF institutions.** The findings reveal the lack of a standardised definition of ISF as well as variations in the types of activities and institutions and their level of development across jurisdictions as well as differences in regulatory and supervisory approaches. Moreover, discussions also revealed a number of challenges and gaps in the regulation and supervision of ISF institutions. While some countries have taken steps to regulate ISF activities, in others there is an absence of dedicated regulations specific to ISF, which often results in reliance on existing frameworks designed for charities, securities, or corporations. This reliance may not adequately address the unique characteristics of ISF institutions, hindering the sector's development and stability.

**The identified gaps and challenges underscore the importance of increasing regulatory and supervisory initiatives to identify policy gaps and ISF specific risks.** Identifying existing barriers and gaps allows for targeted actions and initiatives to address these challenges. Based on the issues that were identified in the paper, a number of areas of focus are highlighted.

- **Regulatory cooperation and coordination:** Regulators currently face challenges due to regulatory fragmentation, as multiple regulatory bodies overseeing ISF operations. The need for complementary frameworks supporting ISF operations may also involve more than one regulator. In light of these challenges, enhancing collaboration and harmonisation among regulatory bodies is a significant factor in ensuring a cohesive and efficient regulatory and supervisory approach.
- **Establishing proportionate frameworks that address specificities of IS:** Addressing the regulatory gaps in ISF may also necessitate the development of proportionate and scalable frameworks considering the scale and characteristics of ISF operations. Regulatory provisions should support innovation without compromising regulatory objectives such as financial stability, integrity, and risk mitigation. Ensuring appropriate governance (including Sharī'ah governance), risk mitigation as well as disclosure and conduct requirements are essential, particularly to strengthen consumer protection in the potentially more vulnerable populations that ISF caters to. While the IFSB has made efforts to address these aspects within the broader context of Islamic finance, specific frameworks tailored to the unique characteristics of ISF are still needed to ensure comprehensive regulation of the sector.
- **Capacity building to address supervisory challenges:** Another significant barrier identified by respondents was the limited expertise and human resources in the technical aspects of ISF supervision. The findings underscore the need for capacity building and specialised training programs to enhance the supervisory capabilities of regulators.

- **Fostering an enabling ecosystem:** Developing an enabling environment calls for a concerted effort involving standard-setters, regulators, government bodies, and ISF institutions. National initiatives as well as regulatory approaches such as innovation offices or sandboxes promotes technological adoption and innovation, while enabling the development of appropriate legal and regulatory frameworks to strengthen integrity, resilience, and stakeholder protection within the ISF ecosystem. This approach would also be beneficial in revising laws and frameworks to accommodate the evolving needs and challenges of ISF.
- **Harmonisation and global benchmarks for regulation of ISF:** The survey respondents highlighted some areas that may benefit from guidance of the IFSB in addressing the specificities of regulating and supervising ISF institutions. This may be particularly relevant to deposit-taking and profit-generating ISF institutions that entail some form of prudential regulation, as well as for those ISF, due to their scale and interconnectivity with the wider Islamic financial system, that pose any financial stability implications.

**The paper has also highlighted the multifaceted nature of the regulatory landscape governing Islamic Social Finance Institutions which can be categorised into two distinct groups.** The first category pertains to non-lucrative ISF institutions, such as *zakah*, *sadaqah*, and *waqf* entities. In contrast, the second category encompasses deposit-taking and profit-generating ISF institutions, including Islamic microfinance, Islamic micro-*takaful*, Islamic cooperatives, and Islamic banks offering ISF services.

**This classification allows for a more comprehensive examination of regulation within the diverse domain of ISF.** Regulation of the first category is less well developed. There is also a question of whether these institutions fall under the regulatory scope of financial sector regulators (where they do not have any implications for the broader financial sector). However, irrespective of regulatory remit, the importance of appropriate governance, transparency, and conduct regulations, including managing conflicts of interest, cannot be overlooked for this group of institutions. The second category of ISF is better regulated. However, some gaps exist, including well-defined recovery and resolution frameworks in the case of failure and appropriate dispute resolution mechanisms.

**In conclusion, developing comprehensive and supportive regulatory frameworks is essential for the long-term sustainability and integration of ISF.** By addressing the evolving needs of the sector and considering the drivers of regulatory change, jurisdictions can create an enabling environment that promotes efficient mobilisation, utilisation, and management of ISF resources while fostering inclusivity and affordability.

## GLOSSARY

<i>Retakāful</i>	An arrangement whereby a <i>takāful</i> undertaking cedes a portion of its risks on the basis of treaty or facultative <i>retakāful</i> as a representative of participants under a <i>takāful</i> contract, whereby it would contribute a portion of the contribution as <i>tabarru'</i> into a common fund to cover specified loss or damage.
Sharī'ah	The practical divine law deduced from its legitimate sources: the Qur'ān, Sunnah, consensus ( <i>ijmā'</i> ), analogy ( <i>qiyās</i> ) and other approved sources of the Sharī'ah.
Sharī'ah non-compliance risk	An operational risk resulting from non-compliance of the institution with the rules and principles of Sharī'ah in its products and services.
<i>Ṣukūk</i>	Certificates that represent a proportional undivided ownership right in tangible assets, or a pool of tangible assets and other types of assets. These assets could be in a specific project or specific investment activity that is Sharī'ah-compliant.
<i>Takāful</i>	A mutual guarantee in return for the commitment to donate an amount in the form of a specified contribution to the participants' risk fund, whereby a group of participants agree among themselves to support one another jointly for the losses arising from specified risks.
<i>Nazir</i>	<i>Waqf</i> institution/administrator (called <i>nāzīr</i> or <i>mutawallī</i> or <i>ḳayyim</i> ). A <i>nazir</i> must have the capacity to act and contract. In addition, trustworthiness and administration skills are required.
<i>Sadaqah</i>	<i>Sadaqah</i> also describes a voluntary charitable act towards others, whether through generosity, love, compassion, or faith.
<i>Qarḍ</i>	The payment of money to someone who will benefit from it provided that its equivalent is repaid. The repayment of the money is due at any point in time, even if it is deferred.
<i>Waqf</i>	A <i>waqf</i> (also known as <i>hubous</i> [حُبُوس] or mortmain property) is an inalienable charitable endowment under Islamic law.
<i>Zakāh</i>	An obligatory financial contribution disbursed to specified recipients that is prescribed by the Sharī'ah on those who possess wealth reaching a minimum amount that is maintained in their possession for one lunar year.

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## APPENDIX: Comparison of Regulatory Practices across jurisdictions

Jurisdictions	Islamic Social Finance Institutions	Responsible Regulatory Authorities	Regulatory Regime	Complementary Regulatory Frameworks	Specific Risks Identified	Specific Disclosures	Supervisory Obstacles	Supervisory Resources and Innovations
Bahrain	<ul style="list-style-type: none"> <li>Islamic Microfinance</li> </ul>	<ul style="list-style-type: none"> <li>Central Bank</li> </ul>	<ul style="list-style-type: none"> <li>Existing regulation</li> </ul>	<ul style="list-style-type: none"> <li>Transparency and disclosure framework</li> <li>Data protection framework</li> <li>AML/CFT framework</li> </ul>	<ul style="list-style-type: none"> <li>Mission drift risk</li> <li>Sustainability risk</li> <li>Credit risk</li> </ul>	<ul style="list-style-type: none"> <li>Must comply with disclosure requirements of Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) and comply with Public Disclosure Module of the CBB's Rulebook for Microfinance Institutions'</li> </ul>	-	<ul style="list-style-type: none"> <li>Not changing</li> <li>Sandboxes and Innovation hubs/offices</li> </ul>
Indonesia	<ul style="list-style-type: none"> <li><i>Zakah</i></li> <li><i>Waqf</i></li> <li>Islamic Microfinance</li> <li>Islamic cooperatives</li> <li>Digital platforms</li> </ul>	<ul style="list-style-type: none"> <li>Government Ministry Departments and Agencies</li> <li>Religious Council or Authority</li> </ul>	<ul style="list-style-type: none"> <li>Existing regulation: Islamic Microfinance and Islamic cooperatives</li> <li>Specific regulations or guidelines: <i>zakah</i> and <i>waqf</i></li> </ul>	<ul style="list-style-type: none"> <li>Donor and recipient protection framework</li> <li>Data protection framework</li> <li>AML/CFT framework</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Integrity risks</li> <li>Technology risks</li> </ul>	<ul style="list-style-type: none"> <li>Annual report on collection and distribution of funds.</li> </ul>	<ul style="list-style-type: none"> <li>Regulatory fragmentation and lack of coordination</li> <li>Limited requisite expertise and human resources</li> </ul>	<ul style="list-style-type: none"> <li>Increasing</li> <li>Digital platform innovation for <i>zakah</i> and <i>waqf</i> collection</li> </ul>
Libya	<ul style="list-style-type: none"> <li><i>Zakah</i></li> <li><i>Waqf</i></li> </ul>	<ul style="list-style-type: none"> <li>Central Bank</li> </ul>	<ul style="list-style-type: none"> <li>Specific regulations or guidelines for <i>zakah</i>, <i>waqf</i></li> <li>Unregulated for Islamic microfinance</li> </ul>	<ul style="list-style-type: none"> <li>International remittance framework</li> <li>Transparency and disclosure framework</li> <li>AML/CFT framework</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Mission drift risk</li> <li>Sustainability risk</li> <li>Integrity risks</li> <li>Technology risks</li> <li>Legal uncertainty risk</li> </ul>	<ul style="list-style-type: none"> <li>Has specific disclosures</li> </ul>	-	-
Sudan	<ul style="list-style-type: none"> <li><i>Zakah</i></li> <li><i>Waqf</i></li> <li>Islamic cooperatives</li> </ul>	<ul style="list-style-type: none"> <li>Financial Services Authority</li> <li>Central Bank</li> <li>Securities Commission</li> <li>Government Ministry, Departments, and Agencies</li> <li>Religious Council or Authority</li> </ul>	<ul style="list-style-type: none"> <li>Specific regulations or guidelines</li> </ul>	<ul style="list-style-type: none"> <li>International remittance framework</li> <li>Data protection framework</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Mission drift risk</li> <li>Sustainability risk</li> <li>Integrity risks</li> <li>Technology risks</li> <li>Legal uncertainty risk</li> </ul>	<ul style="list-style-type: none"> <li>Sources and distribution channels of funds.</li> </ul>	<ul style="list-style-type: none"> <li>Regulatory fragmentation and lack of coordination</li> <li>Limited requisite expertise and human resources</li> <li>Legal uncertainty in legal frameworks</li> <li>Fast pace of technological advancement</li> <li>Limitation of requisite data on the volume of economic activities</li> </ul>	<ul style="list-style-type: none"> <li>Increasing</li> </ul>

Türkiye	-	-	<ul style="list-style-type: none"> <li>Unregulated</li> </ul>	-	-	-	<ul style="list-style-type: none"> <li>Limited requisite expertise and human resources</li> <li>Limitation of requisite data on the volume of economic activities and number of ISF institutions</li> </ul>	<ul style="list-style-type: none"> <li>Increasing Sandboxes and Innovation hubs/offices</li> </ul>
Palestine	<ul style="list-style-type: none"> <li>Islamic microfinance</li> </ul>	<ul style="list-style-type: none"> <li>Central Bank</li> </ul>	<ul style="list-style-type: none"> <li>Existing regulation</li> </ul>	<ul style="list-style-type: none"> <li>Transparency and disclosure framework</li> <li>Data protection framework</li> <li>AML/CFT framework</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Technology risks</li> </ul>	<ul style="list-style-type: none"> <li>Disclosure in the audited financial statements.</li> </ul>	-	<ul style="list-style-type: none"> <li>Sandboxes</li> </ul>
Maldives	<ul style="list-style-type: none"> <li>Zakah</li> <li>Waqf</li> </ul>	<ul style="list-style-type: none"> <li>Government Ministry, Departments, and Agencies</li> <li>Maldives Inland Revenue Authority</li> <li>Ministry of Islamic Affairs</li> </ul>	<ul style="list-style-type: none"> <li>Bespoke or Specific regulations or guidelines for <i>waqf</i></li> <li>Unregulated for <i>zakah</i></li> </ul>	<ul style="list-style-type: none"> <li>AML/CFT framework</li> </ul>	-	-	<ul style="list-style-type: none"> <li>Regulatory fragmentation and lack of coordination</li> <li>Legal uncertainty in legal frameworks</li> </ul>	<ul style="list-style-type: none"> <li>Not changing</li> </ul>
Pakistan	<ul style="list-style-type: none"> <li>Islamic microfinance and micro-<i>takaful</i></li> <li>Available but not considered as formally rendering ISF: <i>zakah</i>, <i>sadaqah</i>, <i>waqf</i></li> </ul>	<ul style="list-style-type: none"> <li>Securities Commission</li> <li>Government Ministry, Departments, and Agencies</li> </ul>	<ul style="list-style-type: none"> <li>Existing regulation and ongoing efforts: Islamic microfinance and micro-<i>takaful</i></li> <li>Unregulated: <i>zakah</i>, <i>sadaqah</i>, <i>waqf</i></li> </ul>	<ul style="list-style-type: none"> <li>Framework for the use of collection intermediaries or agents</li> <li>International remittance framework</li> <li>AML/CFT framework</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Integrity risks</li> <li>Shari'ah non-compliance risk</li> <li>Reputational risk</li> </ul>	<ul style="list-style-type: none"> <li>The Institute of Chartered Accountants of Pakistan has issued the accounting standard for not-for-profit organizations (NPOs) and exposure draft of accounting standard on financial statements disclosures of <i>zakah</i> received.</li> </ul>	<ul style="list-style-type: none"> <li>Regulatory fragmentation and lack of coordination</li> <li>Legal uncertainty in legal frameworks</li> <li>A large number of ISF institutions operating informally outside the formal supervisory perimeter</li> </ul>	<ul style="list-style-type: none"> <li>Not changing</li> <li>Sandboxes</li> </ul>
Philippines	<ul style="list-style-type: none"> <li>Islamic microfinance</li> </ul>	<ul style="list-style-type: none"> <li>Central Bank</li> <li>Securities Commission</li> <li>Philippines Insurance Commission</li> </ul>	<ul style="list-style-type: none"> <li>Specific regulations or guidelines: micro-<i>takaful</i> and Islamic microfinance</li> </ul>	<ul style="list-style-type: none"> <li>N/A</li> </ul>	<ul style="list-style-type: none"> <li>AML/ CFT risks</li> <li>Integrity risks</li> <li>Shari'ah non-compliance risk</li> </ul>	<ul style="list-style-type: none"> <li>None</li> </ul>	<ul style="list-style-type: none"> <li>Limited requisite expertise and human resources</li> <li>Fast pace of technological advancement</li> </ul>	<ul style="list-style-type: none"> <li>Increasing Sandboxes</li> </ul>