

Integrating Faith-based Institutions (Zakah and Awqaf) in Poverty Reductions Strategies (PRS)

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Besides public sector and private sector, there is a third sector in every society that attends to various social needs on voluntary or non-profit basis and non compulsion basis, motivated by philanthropic considerations. Mobilization and development of third sector to fight against poverty is the central theme of the paper. Meeting the needs of poor sections of the society is one of the main concerns of this sector. In Muslim countries and Muslim communities, this sector gets additional strength on the ground of religious norms and obligations. This paper explains the Faith based components of the third sector in a Muslim society and how this sector can be mobilized to generate additional resources to support poverty reduction programs. This discussion is with reference to two main institutions, called Zakah and Awqaf. It has been argued, in this paper, that these institutions have potential to mobilize additional resources for poverty reduction programs and they are required to be included in the poverty reduction strategies by laying down explicit policies to strengthen this sector in the same way as policies are laid down for strengthening the private sector in developing economies. The role of another institution, though not directly a third sector institution, has also been discussed for its potential direct and indirect linkages to the third sector. This institution is called Islamic banking. In the final section, the paper explains, in brief, an initiative taken by Islamic Research and Training Institute, a member of Islamic Development Bank Group to arrange a dialogue among policy makers and planners in IDB member countries, who are preparing PRSPs to discuss how these two institutions can be mobilized and integrated into PRSPs as an additional effort for fight against poverty.

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The Contemporary Global Framework For Poverty Alleviation

PRSP is now the official basis for international financial institutions lending the low-income countries. Many donors are adopting PRSPs as the framework to channel their aid for building coordination around plans that are heavily influenced by the IMF and the World Bank in terms of growth assumptions and poverty reduction approaches. All Highly Indebted poor countries are required to produce a PRSP as a basis for concessionary lending. The World Bank and Fund Boards must approve a country's PRSP before approving a lending program. The role of third sector is discussed in the context of this global framework.

What is Missing From the Poverty Reduction Strategies

Despite a growing heavy bias towards poverty reduction, in the development strategies and development financing, there are a few elements that still remain in these strategies and programs from the point of view of uplifting the economic conditions of extremely poor sections of the society. Some of these elements are worth noting in the context of suggesting the relevant faith based economic institutions to complement the economic policies, strategies and programs for poverty reduction.

1) Additional Resources for Poor Caught in the Short Run Economic Downturn. Despite a claim to shift away substantially from approach formerly known as SAP and making it a strategy directly addressed to poverty reduction, the new approach known as PRSP approach still lacks sufficient ground to fight poverty. Emphasis on macroeconomic stability and structural adjustment is still required to be a core element in PRSP under the guidelines given by World Bank and IMF. And if this is the primary goal then this may often be achieved only at the cost of the poor at least in the short run. And short run is most crucial for the poor people particularly when we are talking about the extreme poverty and starvation. "In the long run, every one is dead". But, in the short run, all those suffering from extreme poverty would be dead, if they are asked to make the sacrifice in the short run for the sake of growth and structural adjustment in the long run.

If additional resources (not currently tapped in the conventional macroeconomic framework) can be mobilized specifically for poor people, then these resources will not require any sacrifice from the poor to finance the planned growth and structural adjustment.

2) Protection of Priority of Social Services Sectors in Resource Allocation

Resource allocation is based on assigning priority to sectors in the poverty reduction strategies. But experience tells that the main victim of the containment of fiscal deficit is generally the social services sector whenever there is an unforeseen shortage of funds. Poverty reduction strategies need to build safety nets specifically for the social services sectors for the poor rather than leaving the poor to suffer along with the rest of the population in the face of resource constraints.

3) Specific Strategy for Eradicating Extreme Poverty and Hunger

The economists in general and economic planners and policy makers in poor countries in particular are not hopeful of significant results from the PRSP approach on the ground that it gives priority to growth. If macroeconomic growth is not achieved, poverty would not be reduced. Poverty incidence, in fact, increased in several Sub-Saharan African countries since the PRSP approach has been implemented there. UNCTAD in its 2003 annual report gave an elaborate review of the PRSP. The report mentions three main points of concern:

- a) The current approach still has the same emphasis on growth and macroeconomic stability that caused deterioration in the poverty incidence.
- b) The anti-poverty policies, though, rightly emphasize the role of education and health, yet this emphasis comes with adherence to the maximum possible extent to market principles for providing these services. This emphasis proves to be counterproductive.
- c) There is still the conditionality element. The aid is linked to fulfilling the conditions laid down (in the guidelines from the World Bank) for structural adjustment and economic growth. Emphasis on macroeconomic stability and structural adjustment may come at the cost of postponing the program of reducing

poverty, at least in the short run, which is most crucial for the poverty stricken population, particularly when we are talking about the extreme poverty.

The most important element missing from PRSP approach is the strategy to specifically deal with extreme poverty and to save people from starvation and hunger. The following points are worth noting in this respect:

The emphasis on strengthening private sector and emphasis on social services like education and health to be provided to the maximum possible extent on market principles leaves the poor stranded on the road to find a ride which may never arrive or may arrive too late. The resources both in the private and public sectors, already pre-occupied to ensure growth and economic stability can hardly set aside any funds exclusively to take care of the needs of the poor through market mechanism and private sector. The poor in general and the extreme poor in particular have no means to fight price hikes that market mechanism and policies of strengthening private sector may lead to in the goods and services needed by the poor, even though the price hike may be temporary and may be expected to slide down as economy develops (in the long run).

PRSPs are required to spell out risk factors in implementing the strategy.

- A) Short fall in public financing to meet the public sector investment targets
- B) Poor domestic revenue performance
- C) Slowing down private investment
- D) Short fall and unpredictability in the flow of foreign aid and private investment

The poor cannot afford bearing the risk. They have no capacity at all to do so. When risk factors are being identified, the PRSP also need to identify what the poor and the extreme poor would do if these risk factors come into force. The PRSP need to provide for the funds to ensure survival of the poor and the extreme poor in case the risk factors come into effect. The sources of such funds will have to be in addition to the resources identified for macroeconomic growth and development of social services. And these resources have to be independent of the resources envisaged in the PRSP for general economic revival and socio-economic development.

Though there is evidence from several countries that economic growth succeeds in reducing poverty incidence¹, there is no concrete evidence to show how much the poor will benefit from a certain rate of growth in the economy. A study for Korea, for example, defined an index called poverty-equivalent growth and indicated that before the East Asian financial crisis the poverty equivalent growth for Korea was 9 percent against the actual growth rate of 1.8 percent (and poverty incidence actually came down from 39.6 percent to 8.6 percent². This implied that the poor had benefited much more from growth in the economy than the non-poor did. The same study then showed that after the financial crisis the actual growth rate in the economy had come out to be much higher than the so called poverty equivalent growth rate. This implied that crisis had affected the poor much more adversely than it affected the growth. **The study pointed out to the need of a permanent system of social safety net to protect vulnerable groups of people.**

Similar prescription is needed for countries faced with extreme poverty such as in the Sub-Sahara African countries. The countries where risk factors identified in the PRSP came into force and the economy faced unexpected down turn, poverty incidence increased and the poor suffered more than the non-poor. The PRSPs do not have any provision of permanent safety nets that will provide the poor necessary support (or save them from starvation) in the face of a draught or short fall in resources or any other unexpected shock to the economy.

In this context, it will be instructive to give the example of Niger. PRSP has been in action since 2000 in Niger. In the end of July 2005, the world suddenly realized the disaster in Niger where millions were facing death due to starvation. This was not the case when a revised PRSP was formulated in the middle of 2004 to ensure macro economic objectives and measures to increase social services for the poor. The poor could not wait for the results promised to them in the long run. They were all dieting in the short period of less than a year.

The bottom line is that the poverty reducing strategy needs to set aside a set of resources not only to counter the negative effect of macroeconomic policies on the

¹ Pasha, Hafiz A. and Palanivel, T. "Pro-poor Growth and Policies: The Asian Experience" Pakistan Development Review, Volume 42, Winter 2003, Number 4, pp 319.

² Kakwani, Nanak and Son, Hyun H., "Pro-poor Growth: Concept and Measures", The Asian Experience", Pakistan Development Review, Volume 42, Winter 2003, Number 4, pp 431.

poor in the short run but also to serve as safety net when the risk factors are in action to thwart the growth in the economy. Since private and public sector resources have already been committed to economic growth and ensuring macro economic performance, the resources to be set aside for the poor in need will have to come from sources beyond these two sectors. **There has to be a third sector exclusively developed for taking care of the poor, while the other two sectors are preoccupied in ensuring rapid economic growth.** This third sector should be an integral part of the PRSP. The PRSP will have to identify specific measures to strengthen the third sector, along with the measures to be identified to strengthen the private sector for the sake of economic growth and the public sector for the sake of macroeconomic management.

Third Sector in Muslim Countries

Third sector is in operation in all civilized societies, in varying degrees and in varying forms. The sector survives and thrives on the philanthropic instincts of human beings. All religions teach taking care of have-nots and less privileged. This makes third sector present in all societies in some form or the other, though mostly in informal form, particularly in developing countries. Muslims, besides having a human instinct for philanthropic activities, also get a lot of inspiration from their religion for taking care of less privileged members of the society. The practical manifestation of this inspiration has been visible through out the Muslim history, in the form of formal institutions. These institutions have played remarkable role not only in reducing poverty but also in the social development of less privileged members of the society. A formal use of the institutions, inspired by religious teachings, to take care of the poor, destitute, and less privileged, has declined in the contemporary setup. These religious commitments and obligations, though, are still strong, yet are being met only informal channels and hence failing to have a visible impact on the society as a whole. There is a need to develop capacity in Muslim countries to best utilize the third sector activities in order to realize their true role in fighting poverty and bringing social development in the lowest income strata of population. Discussion below focuses on following two faith based third sector institutions in Muslim societies that are meant for improving the socio-economic status of less privileged members of the society:

- a) Zakah, an obligatory responsibility of individuals
- b) Awqaf, a voluntary activity with strong religious underpinning

Zakah and Awqaf as Institutions of Third Sector in Muslim Countries and Communities: Concept and Potential

The institutions of Zakah and Awqaf³ are two important pillars of the third sector in Muslim societies. Before discussing the role of these two institutions in fight against extreme poverty and suggestions to incorporate them as a third sector in the PRSPs, the nature and concepts of these institutions and their potential strength in contemporary Muslim societies is discussed below.

Concept of Zakah:

Zakah is a pure religious obligation in the sense that it has to be treated as worship like the obligations of daily five time prayers⁴. But the underlying objective of this institution is to promote social justice and to ensure sustenance to the economically unfortunate sections of the society.

Zakah in fact is an obligation with in a broad featuring the Islamic code of life known as Sadaqat or Infaq or “spending for good causes”. The teachings of the Qur’an and the Prophet (Peace be upon him) lay tremendous emphasis on spending in the way of God out of one’s own resources. Zakah is a minimum obligation under this broad injuncion. There is no upper limit to this spending.

Zakah is treated as a right of the poor and have-nots in the income and wealth of the haves. Broadly speaking, it is to be paid out of the

- a) agricultural produce and live stocks
- b) tangible assets owned (like gold, silver, money)
- c) stocks in trade

³ There are other institutions also besides these too aiming at helping the poor and have-notes of the society. Obligatory spending on parents and grand parents, for example, are not mentioned here as they are now commonly being treated under one’s own needs or as family spendings. There are several other provisions. Zakah and Awqaf, however, have been reflected for discussion being the two main elements of the third sector.

⁴ Obligation to pay Zakah has been mentioned 30 times in the Quran, of which 20 times it has been mentioned with the obligation to establish daily prayers.

Every Muslim having resources beyond a certain limit (which is very low) has to pay Zakah on annual basis. The low limit on the ownership of resources that qualifies the owner to discharge Zakah obligation is meant to keep a broadened base to generate resources for the poor. The rate at which Zakah is to be paid out of one's resources is also too low (which is only a reflection of the objective for encouraging the payment).

Injunctions are very strong relating to the payment of Zakah obligation:

The Qura'n says, "..... And there are those who hoard gold and silver and spend it not in the way of God; announce unto them a grievous penalty. On the Day when heat will be produced out of that (wealth) in the fire of Hell, and with it will be branded their foreheads, their flanks and their backs [and it will be said to them], "This is what you hoarded for yourselves; taste ye, then, what you hoarded". (IX: 34-35) and also "whoever saved a life, it would be as if he saved the life of the whole humanity" (V: 32).

The Prophet (peace be upon Him) is reported to have said: If a single person were to sleep hungry [Muslim or non-Muslim] in a town, God's protection is lifted from such a town (Masnud Imam Ahmed).

Zakah is an obligation related to defined types of property from which a part is to be paid every year to the poor as their right. There is a minimum amount of property to be owned in order to qualify as payer of Zakah. Zakah will be payable only if one owns the property beyond that limit. This limit is called Nisab. There is a minimum amount that becomes due to be paid every year. Table 4 shows the Nisab (minimum amount of ownership of different kinds of property, beyond which owner becomes liable to pay Zakah) along with the minimum rate of Zakah to be paid. The table is only indicative of a broad picture about the structure of Zakah obligations. For a detailed and precise description of this institution, see Qardhawi (2).

Table 4
Nisab and Rates of Zakah
For Some of the Contemporary Items

	<u>Rate</u>	<u>Nisab</u>
Cash	2.5%	Equivalent of 85 Grams of Gold
Bank Deposits	2.5%	Same as for cash
Stocks in Trade	10%	Same as for cash
Agricultural Produce	5%, if investment is made in inputs and irrigation (10 percent otherwise)	653 KG
	10%, if there is cost of inputs	no
Real Estate	2.5% from their income	
Professionals	2.5% from their income after deducting cost	
Shares/Stocks	10% When dealing in the Trading of Shares	
	2.5% from income if for the purpose of investment	

Note: Zakah is paid once in one year on such property that on which one year has passed while in the possession of the owner.

Zakah in Islamic History

Zakah, in fact, created the first universal welfare system in human history. The economic system that emerged when Islam took hold in the Arabian Peninsula was a reflection of what is known in the contemporary world as welfare economy. There was a time in the early history of Islam, which is recognized by contemporary

historians also, when hardly any one was in need of charity. Muslims were finding hard to locate poor and hungry in order to discharge their religious obligations of paying Zakah.

Throughout Islamic history, Zakah collection and distribution have been among the functions of Muslim governments. This has been the case until the end of Ottoman empire. Besides government, Zakah during all this period has been managed through other institutional arrangements as well, notably like Awqaf (Trust) organizations.

Zakah is, in principle, an individual act like saying prayers five times a day. But like prayers, being preferred collectively, Zakah too has been preferred to be managed collectively, rather than individually. The fact that Qura'n allows part of Zakah collection to meet the expenses on the management of Zakah, implies a religious encouragement for making an institutional encouragement to manage Zakah.

Despite that the practice and application of Islamic injunctions have deteriorated considerably over time, payment of Zakah is still carrying significant importance in Muslim's daily life, sometimes even more than the importance given to other injunctions like daily 5-time prayer or annual fasting in the month of Ramadan. This is partly reflected in the donations given to NGOs and charitable organizations working for the poor in Muslim societies⁵. But the donations to charities and their injunctions form a rather small part of the Zakah obligations constantly discharged by Muslims in their societies through personal and informal channels. In most cases, these channels may not be serving the purpose of fighting poverty (as they are paid to so called professional beggars in public places who may not necessarily be "poor").

In contemporary societies, NGO organizational type set-up is considered more suitable for Zakah management on grounds already discussed. Some contemporary Muslim governments, however, are taking the responsibility of collecting and distributing Zakah. An overview of the formal administration and management of Zakah in some contemporary Muslim countries and societies is given below:

⁵ For example, it is estimated that it \$700 million, are mobilized annually through charities in Pakistan. This 10 times more than what is deducted, by law, from the banking system, as official deductions for Zakah. (Christian Science Monitor, November 15, 2005)

Zakah Management in Some Contemporary Muslim Societies

Yemen is one of those few countries where government continued to manage Zakah collection and distribution even after the fall of Ottoman empire. Currently, Saudi Arabia, Malaysia, Libya, Pakistan and Sudan are the major Muslim countries having enacted laws for government bodies to formally collect and distribute Zakah.

These countries make provisions, in the law, making it obligatory to pay Zakah on some specific items, defined in the law, to bodies created by the government while the Zakah on other items, not specified in the law, is left to be voluntarily paid either to government body or elsewhere.

On the other hand, there are countries where government has established institutions to collect and manage Zakah only voluntarily contributed by Zakah payers. These countries include Bahrain, Bangladesh, Egypt, Indonesia, Jordan, Kuwait, Oman and Qatar. Majority of the contemporary countries, however, leaves it entirely to the private (charity) organizations or NGOs to manage the collection and management of Zakah. There is no country, where all Zakah obligations are made to pass through formal channels (whether government bodies, or NGOs or charity organizations). In all countries a substantial amount of Zakah passes through informal and unorganized or personal channels that hardly have the capacity to ensure that the Zakah contribution is effective in alleviating poverty in their societies.

It may be noted that Zakah is a right of have-nots in the wealth of haves. It has to be given to the poor as their right and not as a favor to them and it is received by the poor as their right and not as a favor. It is an obligation to be discharged with no reward or return in this world. The reward is expected only in the Hereafter. The people intending to pay Zakah thus try to make sure that it reaches those who are poor so that the Zakah payers can expect a return in the Hereafter. Hence, either they themselves would like to pay it to those whom they know that they are the poor, deserving to receive Zakah, or they give it to a third party, an institution, whom they

have trust that they are in touch with the poor and would pass on their Zakah money honestly to those whose needs are meant to be met out of Zakah. It is for this reason that government bodies, in contemporary set-up may not often be preferred by Zakah payers to manage their Zakah. The track record of NGOs have been better in this respect.

The most important reason to organize formal management of this institution at community level, national level and global level in the contemporary socio economic set-up is the permanency of this institution to generate predictable and stable resources for meeting the needs of the poor. As an additional resource for poverty alleviation, this source is not vulnerable to short term fluctuations in the economy. This is, firstly, because the base is very wide. Even small households of small incomes like to contribute for religious reasons. Secondly, temporary setbacks in the economy and economic conditions of individuals may not immediately be reflected in the reduced Zakah contributions, again because of religious considerations and commitments. Small fluctuations in the economy and its performance though may reduce funds from public sector, private sector and foreign donors for poverty alleviation programs, the programs run on the basis of Zakah and sadaqat money may not be affected to the same extent. People still like to stick to their regular commitment towards the poor even if they have some short term setbacks in their businesses or incomes.

Some studies conducted in Muslim countries indicate the following potential of Zakah. As there is juristic differences on rate of Zakah and Nisab on certain items, the Zakah potential has been shown under three main juristic views.

Table 5
Estimate of Zakah potential as Percent of GDP

Country	View 1	View 2	View 3
Egypt	2.0	3.9	4.9
Indonesia	1.0	1.7	2.0

Pakistan	1.6	3.5	4.4
Qatar	0.9	3.7	3.2
Saudi Arabia	1.2	3.7	3.4
Sudan	4.3	6.3	6.2
Syria	1.5	3.1	3.1
Turkey	1.9	4.9	7.5

- M. Kahf, “Zakah: Unresolved Issues in the Contemporary Fiqh”, in *Majalat Abhafh al-Iqtisad al-Islami*, vol. 2, No. 1, January 1989, pp. 16-18.
- M.A. Zarqa, “Nuzum al-Tawzi’ al-Islamiyyah”, in *Majalay Adhath al-Iqtisad al-Islami*, vol. 2, No. 1, 1984, p. 23.
- Fuad al-‘Umar, “Taqdir Hasilat al-Zakat fi Mujtama’ Islami Mu’asir: Halat al-Kuwait”, presented to the Fourth International Zakat Conference, Senegal, March 1995.

No country, however, is reported to have collected the Zakah to the full potential mentioned above. According to some other views, these estimates seem to be far conservative. A study conducted in 1980s on the basis of UN statistics on national accounts in eight oil producing countries and 10 non-oil producing countries concluded that oil producing countries can potentially collect 10 to 14 percent of their GDP as Zakah and non-oil producing countries can collect 3.5 to 7 percent of their GDP as Zakah.

Awqaf

Awqaf (plural of Waqf) is an important institution of Islamic civilization aiming at taking care of the needs of the society that are otherwise ignored in the process of economic growth and development. This is an institution that helps social development keeping pace with economic growth in the society.

Waqf represents a property dedicated in perpetuity for specific beneficiary to achieve specific objectives. The motivation of establishing such as institution is the same as that of Zakah mentioned in the earlier section. The only way in which it differs from Zakah is that it reflects spending in the way of God beyond what is minimum obligated in the form of Zakah. Since there is tremendous rewards promised in the Quran for spending in the way of God, there is a strong urge among the believers to spend as much as one can after meeting his and his family’s own needs. One motivation to spend in the way of God by way of forming a (a Trust) is that this continues to generate rewards (thawab) for the initiator of the even after his death. As long as the is operational and benefiting the beneficiaries, its rewards continues to flow to the soul of the deceased. It is by this virtue that it falls into the category of Sadaqah Jarriyyah (a good deed that continues even after death).

It is this motivation that has kept this institution not only alive and active throughout Islamic history but has contributed significantly to various social causes such as health, education, research and meeting needs of less privileged/poor sections of the society.

In the contemporary set-up, this institution, however, has ceased to play its effective role on account of various reasons. Instead of counting the factors, not allowing this institution to play the role that it has played in the history, it will be more useful for the purpose of this paper to give an overview of the current state of this institution in Muslim countries and giving a broad vision of what can be done to revive this institution with particular focus on its role in alleviating poverty.

Current Situation

The current state of Awqaf has the following two remarkable features:

Firstly, there is a huge stock of Awqaf property lying in various parts of the world (Muslim as well as non-Muslim) which have been abandoned and are no more operative. These properties are simply lying idle. Since the ownership of these properties cannot change, nor these properties can be inherited, the contemporary legal structures in the countries where these properties are lying, does not have adequate provisions to revive these properties allowing them to operate for the purposes for which they were created. A large stock of Awqaf property is lying idle even in Muslim countries where legal structure recognizes the nature of these properties but there is no arrangement to take stock of these properties and re-organize and revive them to operate effectively. Because of the absence of physical owners, countries find it difficult to take any step towards the development of such property. Recently, some countries (examples, being Saudi Arabia, Pakistan, Kuwait) have taken concrete steps to organize and revitalize the awqaf properties, inherited from the past, currently lying idle or being misused. Specific Ministries and departments have been established for this purpose. Attempt is being made to develop financing schemes for developing these properties without compromising the principles of Awqaf. Islamic Development Bank (IDB) has played an important role

in providing financing for developing idle Awqaf properties in some countries. The Islamic Development Bank has gone even a step further. It has established a World Awqaf Foundation which seeks to preserve and develop Awqaf in conformity with its target not only to contribute to the socio economic development of Muslim countries but also to alleviate hardship faced by the poor sections of Muslim societies. This will be done in cooperation with the national Waqf societies and organizations as well as with the support and coordination among the institutions of the civil society in Muslim countries and Muslim communities. Financing the programs to revive Awqaf properties lying idle or underutilized will be one of the main activities of the Foundation.

The establishment of this Waqf Fund realizes the fact that many philanthropists of the Muslim world are eager to meet social needs in Muslim countries and Muslim communities but they need a mechanism to preserve their Waqf properties and to enable them to spend the proceeds as they wish. IDB World Waqf Foundation would attract Waqf funds to participate in assisting charitable projects in IDB member countries and Muslim communities in non-member countries.

Secondly, not only that considerable number of Awqaf properties inherited from the past are lying idle, but also the new Awqaf are not coming up particularly to alleviate hardships faced by the poor despite potential capacity among the wealthier population in Muslim countries and communities. The main factor thwarting the emergence of new Awqaf institutions is the absence of legal protection to the Awqaf property. The legal system of property rights in many Muslim countries is not only weak but also whatever system exists is not properly enforced. These weaknesses in the system of property rights are detrimental to the growth of private sector as well as third sector and Awqaf development.

Perspective on Awqaf Development as an Instrument for Poverty Alleviation

The institution of Awqaf, in the contemporary socio-economic set-up should be seen as an additional source to support the program relating to poverty alleviation. The past history of Awqaf suggests that this institution can be used to mobilize additional resources for poor sections of the society.

- a) Education.
- b) Skills and micro entrepreneurial development
- c) Health care and care of HIV/AIDS infected population
- d) Water and sanitation facilities in rural areas

Awqaf can also maintain a fund properly invested which can be utilized in periods of famine and other crisis to help extreme poor to survive the crisis or the famine.

In the context countries with extreme poverty, new Awqaf can come to help the people in extreme poverty facing starvation, death and diseases. This potential, however, can be harnessed only by providing appropriate legal protection and supportive environment. Creating awareness among the affluent members of society as well as Muslims abroad about the need and usefulness of establishing Awqaf institutions in Muslim countries with extreme poverty can mobilize a lot of funds for the establishment of Awqaf for fighting poverty.

Role of Islamic Financial Institutions

Though Islamic banks and other Islamic financial institutions do not fall into the category of the third sector institutions, yet development of Islamic financial sector as faith based institution, may prove as a useful institutional link between the Zakah payers and Zakah receivers. Islamic banks may provide the services of collection and distribution as a part of their own operational programs. These services

can be utilized by government and NGOs also to provide social services meant for the poor only. Islamic banking can also help mobilizing idle savings which remain outside the conventional banking system because of its involvement in the interest which is abhorred in the religion. These additional resources mobilized through Islamic financial institutions can be used for the investments that would directly and indirectly benefit the poor.

Besides, providing a service to collect and distribute Zakah and mobilizing household savings that would otherwise remain idle in the form of cash or jewelry or precious metals, the Islamic financial institutions also have the potential to directly benefit the poor from its own operational activities. There are three main operations of Islamic financial institutions already in practice for the purpose of alleviating poverty.

1) **Qardh Hasan Institutions:** These institutions successfully operating and growing in Iran are in the form of revolving funds contributed by the affluent members of the system to be advanced to the poor as an interest free loan to either improve their business or to meet some emergency consumption needs. The money given to the poor as a loan is returned back as per agreement and becomes available to be lent to other needy people. Such an institution is particularly useful in situations where an unpredicted climatic condition in drought has created a crisis situation leading to starvation. Qardh Hasan helps them survive during the crisis situation, while the loan is returned back once the crisis situation is over. In normal times, Qardh Hasan is used to provide capital to the poor to uplift their economic status.

2) **Risk Bearing Capital Provisions:** Islamic banks operating on commercial basis may not extend Qardh Hasan, but they can still be instrumental in helping the poor to uplift their economic conditions. They can provide risk bearing capital to the poor for their entrepreneurial activities. The banks will share the profit that they make from the capital of the bank and the bank will bear the loss, in case the entrepreneurial activity loses part or all of the capital. This model has been successfully operated for last several years by Islami Bank Bangladesh Ltd. and succeeded in pulling numerous poor families out of the poverty trap.

3) **Operating a fund to achieve some specific objective towards improving the economic condition of poor:** Tabung Haji, a successful fund operating in Malaysia to manage the to help people of small means to discharge their Haj obligation⁶ by giving them opportunity to make regular small savings over the life to accumulate their Hajj expenses. In this model, the people of small means deposit affordable savings regularly with the organization of Tabung Haji, which undertakes to arrange for them the entire journey and bear the entire cost for performing Haj. Tabung Haji invests the regular contributions received from the people in useful projects and hence performing dual functions: a) mobilizing resources for investing them in the economy and b) enable people of small means to perform Haj. This model can be replicated for several purposes, particularly for the needs of the poor. For example, such a fund can be established to provide turnkey business projects for the poor but skillful people, to provide better housing, to promote education of children, etc.

Including Zakah and Awqaf in PRSPs

For countries with substantial Muslim population, there is a strong case for macro-economic framework as well as national accounting frame work to define variables for third sector both on the side of “Resources” as well as on the side of “Uses of Resources”. This third sector is neither private sector, nor public sector but it is a sector which is substantial and is keen to discharge its responsibilities towards the poor as a part of religious obligations. It is neither motivated by profit/commercial considerations, as in private sector nor coerced by state legislations (such as tax obligation which carries temptation for evasion and avoidance). This is a sector that takes care of the needs of the poor for no reward in this world and even without being recognized .

How relatively big this sector is in countries with substantial Muslim population, is an empirical question. There is no reason why empirical studies should not be rigorously pursued in the interest of streamlining macroeconomic policies with emphasis on reducing poverty and strengthening reformulation of macroeconomic

⁶ Muslims are obliged to perform once in life time a pilgrimage to Makkah. This pilgrimage is a costly affair for people of small means living far away countries.

framework to redesign poverty reduction strategies not only to attract funding from World Bank and IMF but also to strengthen the third sector to enhance its capacity to poverty reduction while strengthening private sector and public sector to contribute to economic growth and socio economic development. Some countries may require technical and financial assistance to institutional building and capacity building.

The present framework for PRSPS, however, cannot be used to determine how much the poor have benefited from these organizations and how much resources have been mobilized by these organizations through philanthropic and religious considerations. This framework, also does not help with respect to the way how this sector can be strengthened to enhance its role in poverty alleviation. There is a need to review the entire Standardized National Accounts (SNA) framework for poverty stricken countries to orient it towards not only economic growth and enhancing the role of public and private sector in that respect but also towards poverty alleviation and the role of public sector and third sector in that respect. However, at this stage the suggestion is confined to the way in which the existing SNA framework for this purpose could be utilized.

First step would be to streamline the national accounts statistics that provide the bases for macroeconomic framework. The following statistics need to be compiled through Household Income-Expenditure Survey:

- i) Population below poverty line.
- ii) Household income of population below poverty.
- iii) Consumption expenditure of households below poverty line.
- iv) Consumption (current Expenditure) of private non-profit institutions serving households below poverty line.

The Standardized National Account (SNA) define “Private Non-Profit Institutions Serving Households” as institutions, not mainly financed and controlled by government.

In principal, this category of “Private non-profit institutions serving households” can include the NGOs that are providing services to the households out of Zakah contributions or out of Awqaf resources. But the item, “Private non-profit institutions serving households” in the SNA framework is reflecting only the

administrative expenditure on the activities carried out by the institutions of the third sector. Member countries that currently have the information on this category, can have some assessment of the role of the third sector in poverty alleviation from the figures in this category. The source that provides this information is supposed to have the information about the amount spent on the households by these institutions in meeting their various needs.

Most of the countries in the region, however, currently do not have this item in their national accounts probably because of non-availability of data. This in turn probably would be either

- 1) due to lack of registration of such institutions or, if institutions are registered then,
- 2) due to lack of mechanism to receive the required data or, if the data is received then,
- 3) due to absence of system to incorporate the necessary data into the national accounts

The following is proposed to include this item appropriately in the national accounts.

Countries may register all Private (non-government) non-profit Institutions/NGOs that work for the poor and identify those that receive zakah contributions as a source of funds for their activities.

Firstly, the registration is to be mandated for all such non-profit organizations that serve households. The registration must require information on their sources of funds, particularly those related to Zakah (including Ushr and Sadaqat).

The first step in this direction would be collection of statistics and estimation of basic parameters reflecting the existing status of third sector in the economy. Those countries that already have programs to conduct household income-expenditure surveys, this will only require modifying some existing questions and/or adding new questions to get the required data. For those countries that do not have household income-expenditure surveys, it will be more useful for them to design the entire survey with a clear focus on obtaining required data to help formulate an effective poverty reduction strategy (PRS).

International donor institutions like World Bank, IMF and UNDP, Asian Development Bank, African Development, Islamic Development Bank may also consider joining hands with national bodies to build up the required data base.

With respect to statistics on capital formation which are normally collected through government agencies registering and/or supervising investment activities, it is needed to compile statistics separately on the investments made by the third sector organizations like Awqaf, NGOs etc. and to include them separately in the macro framework under the headings of Fixed Capital Formation Promoting Awqaf Activities through appropriate policies.

The Muslim countries may also need help in building up capacity in the third sector, particularly those relating to Zakah and Awqaf. In order to allow these institutions and other third sector activities to play their role effectively in poverty alleviation, appropriate policies and legal infrastructure for their protection and promotion is needed. Legal framework is needed to formalize the collection of philanthropic as well as religious dues for the poor (like Zakah) and their distribution among the deserving. Since there is already strong will present in the public to contribute resources to support Zakah and Awqaf based activities, besides the strong will to give time and work effort for the poor in the community⁷ (to provide the reference) as a religious norm, the focus of public policy will be required to be

- i) facilitating the establishment of institutional framework for these activities
- ii) supervising, monitoring and regulating the activities to minimize misuse of the institutions and of the resources mobilized by them
- iii) developing legal and institutional infra-structure to facilitate the institutions to carry out their activities in fighting hunger, disease and poverty.

Macroeconomic framework also needs to identify resource gap specific to poverty reduction and independent of the resource gap for economic growth and development. This gap can be shown below the line (of the standard Macroeconomic

⁷ It is reported that 58 percent of Pakistani, in working age (15 years of age and above) volunteer a part of their time to the needy causes (The Christian Science Monitor, November 15, 2005)

framework) as shown in Table 5. The resource gap for poverty reduction is to show the following elements:

1. Resources required to achieve the planned reduction in poverty incidence. This is an exercise to be done by the planners on the basis of the population living below poverty line and the targets laid down in the plan for alleviation of the poverty.
2. Income and resource transfers to the poor households. These will require statistics to be compiled with respect to
 - a) voluntary Zakah and similar contributions to the poor
 - b) Zakah and similar payments made to the poor out of obligatory Zakah collected by government institutions or out of governments owned fund for social security
 - c) transfers made to the poor or needs of the poor through the operations of third sector institutions (Awqaf, NGOs etc.)

While statistics (b) and (c) can be done by streamlining the reporting procedures of the concerned institutions, the statistics of voluntary contributions will require a separate household survey or can be made part of the existing Household Income-Expenditure Surveys.

Role of State

It has been argued that direct involvement of state in organizing and managing the institutions of Zakah and Awqaf may not lead to an optimal mobilization of resources from these institutions. There are serious apprehensions expressed in different national and international fora about the governance issues among the public and hence a factor leading to reluctance of the public to hand their Zakah and charity funds to government institutions⁸. The effective role that state can play in this respect is creating enabling environment, providing supporting legal framework and protecting property rights through effective enforcement of law. The role of state in promoting the third sector (particularly Zakah and Awqaf institutions) thus should be

⁸ This view has been expressed also in the report of World Faith Development Dialogue included in the World Bank study by Marshall and Keough [8].

similar to the one the state assigns itself in PRSPs for developing, promoting and strengthening the private sector.

Potential of Zakah in Reducing Poverty Incidence

The poverty incidence in Sub-Sahara African IDB countries ranges from 25 percent to 75 percent. For the purpose of reduction of extreme poverty a rough exercise has been shown below to the potential of Zakah and other charities for reducing at least the extreme poverty and bringing those below poverty line (of earning \$1.00 per day) to at least getting one dollar per day.

Assuming on the average 30 percent of the population below poverty line being extremely poor, two strategies have been used to make some broad calculations. First, reducing extreme poverty in three years' time by contributing \$ 0.70 per capita per day to all the population below poverty line through Zakah funds. Second, reducing extreme poverty in five years' by contributing 0.5 dollars per head per day. Only a few countries' example is shown below to make the point. The figures calculated below may be seen in the perspective of total Zakah potential shown in table 5 as calculated by different research studies.

Realization of Zakah Potential

Contemporary institutional arrangements for Zakah collection in order to enable its planned disbursement for the purpose of eliminating of extreme poverty takes different forms in different countries. Many countries leave it purely to individuals' private arrangements. In such cases, normally NGOs and charity organizations play a greater role in organizing the Zakah collection and disbursing to the needy as well. Other countries make it a combined effort of public sector, private sector and third sector. The Public sector would be collecting Zakah on some specified Amwal Zahira (Zakatable properties easily identifiable) while leaving Zakah on all other categories of properties to private arrangements and to NGOs.

Compulsory deductions of Zakah by government in Pakistan is mainly on the bank deposits. A specific date is declared for the deductions of Zakah and on that date the bank deposits are subjected to 2.5 percent Zakah. Those who thought their deposits were not subject to Zakah like (non-Muslims or that their deposits have not been there for complete one year etc) could make a representation to the government in this respect and could get the Zakah collected from their account reimbursed to them.

Initially there was apprehension that people who did not wish government to make Zakah deductions would be taking out their money before the date of deductions and thus leaving very little or nothing for the government to collect. It was also apprehended that this will be detrimental to the public confidence in the banking sector. However, these apprehensions did not come out to be true. Very little withdrawals were made from the banking system on the date of Zakah deductions. Government was thus able to collect Rs. one billion or 1 percent of GDP. The Zakah collections by government have continuously been increasing since then on an average rate higher than the annual growth in GDP.

Government of Pakistan also created an elaborate network of committees at national, regional, and local level to distribute Zakah to the needy. The main focus is the extreme poor population. Mosques were utilized for forming committees at local level as people coming to mosque would know better who in the neighborhood is extremely poor. Zakah payments contributed 39 percent to the disposable income to the recipients of Zakah in the lowest income decile⁹. This system is operating quite successfully for more than 20 years.

Similar experiences have been found successful in several gulf countries. These experiences can be replicated in sub-Saharan African countries too. Even if one percent of GDP can be mobilized from Zakah it raises substantial additional funds to fight extreme poverty. If government's carefully designed network supplemented by appropriate policies for promoting NGOs and charity organizations are put in place

⁹ Shirazi (11) pp 345.

for collection of Zakah, additional resources thus mobilized to fight extreme poverty may exceed 1.5 percent of GDP in most of the Sub Sahara African countries.

Policies for mobilizing the required potential and disbursing it to the poor

Sub-Saharan African countries can learn a lot from countries like Pakistan and those in the Gulf region how to collect Zakah through banking channels and from the formally organized business sector. The transparency in the collection and utilization of funds thus mobilized will be the key to success. Besides using government machinery, enabling environment created for voluntary organizations (Third sector organizations) to collect and distribute Zakah will also be able to mobilize Zakah and charities for putting an effective fight against poverty. The voluntary sector will not be competing government channels to collect Zakah from the same source. Government channels will be collecting Zakah mostly from what is called Amwal zahira (property known to government like bank deposits, shares in the corporate sector etc). Government will not be able to collect Zakah on what is known as Amwal Batina (properties not known to government like jewelry, gold or silver or cash at home or in informal channels etc.). But people do give Zakah on such property as well but only through personal contacts. Trustworthy NGOs and charity organizations can effectively mobilize Zakah collection from such property which may potentially be higher than what government can mobilize. Enabling environment for the Third sector organizations to play effective role will require appropriate legislations particularly those dealing with protection of property rights and governance rules for the Zakah collecting organizations.

Consumption Subsidy or Financing Capacity Building

There is a debate that if Zakah is collected through institutional arrangements then should it be given as consumption subsidy or should it be used to build up the capacity of the poor to improve their economic conditions and economic status. For the extreme poor faced with starvation and death and disease, this debate is hardly relevant. The Zakah has to be used to meet their immediate survival needs. However, as poverty alleviation strategy, this question becomes very important. Building capacity of the poor through health, education, vocational training facilities etc will

help them to get out of the poverty trap. It is not objectionable in Islamic law if these facilities are provided through Zakah funds provided these facilities are meant only for the benefit of the poor. Such facilities, however, have been generally provided under the umbrella of a organization rather than under the umbrella of government transactions. Government institutions are normally considered to be having higher overhead and administrative expenses and also often there are transparency issues in the use of funds. Entrusting government with the Zakah money to provide the facilities is not considered an efficient use of Zakah funds, while Zakah payers have been found reluctant to give Zakah to government for such purposes. Third sector has been found playing effective role in this respect in several Muslim countries.

Third Sector Role in the Capacity Building of the Poor

Awqaf generally have been found with good reputation in providing such services. Also Awqaf bring their own money to establish the institution and become a source of additional funds to serve the cause of poverty alleviation. Potentially there are substantial funds in every Muslim society willing to be devoted to establish property. The absence of proper legal infrastructure (particularly the legal system of property rights and lack of its effective enforcement) however often is the obstacle. Creating an enabling environment can attract substantial funds for establishing Awqaf institutions for poverty alleviation particularly in Sub-Sahara African countries where the poverty incidence is the highest in the world. World Waqf Organization has been established recently by IDB to mobilize support and sponsor Waqf institutions with specific emphasis on health, education and other social services. Sub-Sahara African member countries of IDB may seek the support of WWF to organize and promote Awqaf institutions in their respective countries and hence attract additional resources beyond what is provided in PRSP for poverty alleviation. WWF may also provide help to member countries in enacting effective legislation. A proper legislation to help the establishment of Awqaf institutions can also attract NGOs from abroad to work for capacity building in the poor sections of the society.

Role of IDB/IRTI

IDB has always been conscious of the poverty incidence in its member countries and particularly in Sub-Saharan African member countries and of its obligations to play its role to help the countries in their fight against poverty. It has launched during 2000-2001 a special program on strengthening Zakah and Awqaf institutions as a means for building capacity to alleviate poverty. It has also provided financing to help some member countries to revitalize some of their Awqaf property that were lying idle and unutilized.

IDB has also established a Trust Fund known as World Waqf Foundation (WWF) to achieve the following objectives with respect to the development of Awqaf in IDB member countries and in Muslim communities in non-member countries:

- a) to support the establishment of a network of institutions that would perform Shariah compatible charity activities,
- b) to sponsor and support institutions, coordinate their activities and prove them with expertise,
- c) to extend assistance to students and provide scholarships in disciplines that can fulfill the needs of the Ummah,
- d) to establish and support educational, health and social institutions and programs,
- e) to contribute to the alleviation of poverty so as to enable peoples of the world to overcome hardship and build their capabilities,
- f) to provide relief aid in the form of goods and services,
- g) to help IDB member countries to enact uniform legislations.

Islamic Research and Training Institute not only has published a lot of material in creating awareness about these institutions¹⁰ but also has conducted training programs in the Sub-Sahara region. IRTI has provided technical assistance also to help them establish Zakah institutions. IRTI will continue providing training

¹⁰ These publications can be seen at the website www.irtipms.org or at www.irti.org

programs and technical assistance for establishment of such institutions as and when such requests are received.

IRTI Working Group of Poverty Alleviation

A recent initiative taken by IRTI in this respect is the formation of a working group for Sub Sahara African member countries. The group consists of senior government officials directly involved in preparing PRSPs. The Working Group was established with following specific objectives.

- To provide a forum to IDB member countries for a dialogue to discuss the policy options, identify best practices and explore cooperation among member countries to mutually achieve the targets for reducing extreme poverty in their countries.
- Help member countries in adopting policies and strategies to best utilize the domestic and international resources available for poverty alleviation including Zakah and Awqaf.
- Create awareness among development partners and member countries of the usefulness of Zakah and Awqaf as effective tools to fight poverty.
- To provide feedback to IDB Operations Complex on issues related to poverty alleviation in member countries.

The Working Group, initially focused on serving as a forum for dialogue among member countries on the role that Zakah and Awqaf institutions can play in the region to wards fight against poverty. The first meeting of the Group was held in May 2006 focused only on this issue. The participants generally agreed to integrate such faith based concept in the preparation of their PRSPs, though it was realized that it may take time to develop capacity to benefit from such institutions. The IRTI working group will continue to meet for further deliberations on this dimension of the fight against extreme poverty.

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