

*Research Fellow Seminar Series  
Centre for Islamic Economics*

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**Framing the Social Responsibility Role of  
Islamic Financial Institutions  
Within A Three-Sector Economic Model**

# BACKGROUND

Contentious debate on the SR role of IFIs  
Consistent call for IFIs to shoulder SR roles  
Increasing acceptance of SR role among IFIs

However, there is an absence of a macro model that can be used to conceptualise the potential interaction between the different sectors in the economy in relation to social welfare issues

# Objectives

To examine the debates on SR role of IFIs in the economy and reflect this using the framework available in the three sector economic model literature.

To frame the SR role of IFIs within a three-sector economic model

# Organisation of the Paper

After this introduction...

2. Debates on the SR roles of IFIs
3. Framing the debate- Reflecting from the literature of 3-sector model
4. An Integrative Framework for Social Welfare Provision
5. Framing the SR Role of IFIs
6. Conclusion

## 2. The Debates

The emergence of Islamic banking was touted to be the operational aspect of Islamic economics in realising its normative goals

Justifications for the SR roles of IFIs:  
micro foundational assumption of homo Islamicus  
principles of Islamic moral economy  
the theory of Maqasid

## 2. The Debates

The Chapra model (Lewis and Algaoud, 2001: p. 95; Chapra, 1985)

As organisations operating within the domain of the Shari'ah, IFIs must not operate solely on profit motive, but are also expected to assist in the promotion of social justice and overall human wellbeing in line with the objectives of the Shari'ah.

## 2. The Debates

The Ismail (2002) model

As a constituent of the 'commercial' sector, IFIs should operate as a commercially viable provider of *Shari'ah*-compliant financial services without being burdened by various social and welfare responsibilities.

Classifies the economy into three distinct sectors; government/public, market or commercial, and the philanthropic, welfare or the third sector.

# 3. Framing the Debates

Reflects the ongoing debate and explores the potential of bridging the dichotomy between the three main sectors in the economy.

Two dominant models defining the third sector and specifying the interaction between the third sector with other sectors in the economy.

The American model

The European model



# 3. Framing the Debates

The American model

Study done by John Hopkins Comparative Non-profit Sector Project (JHCNSP).

5 characteristics of TSOs based on a structural-operational approach:

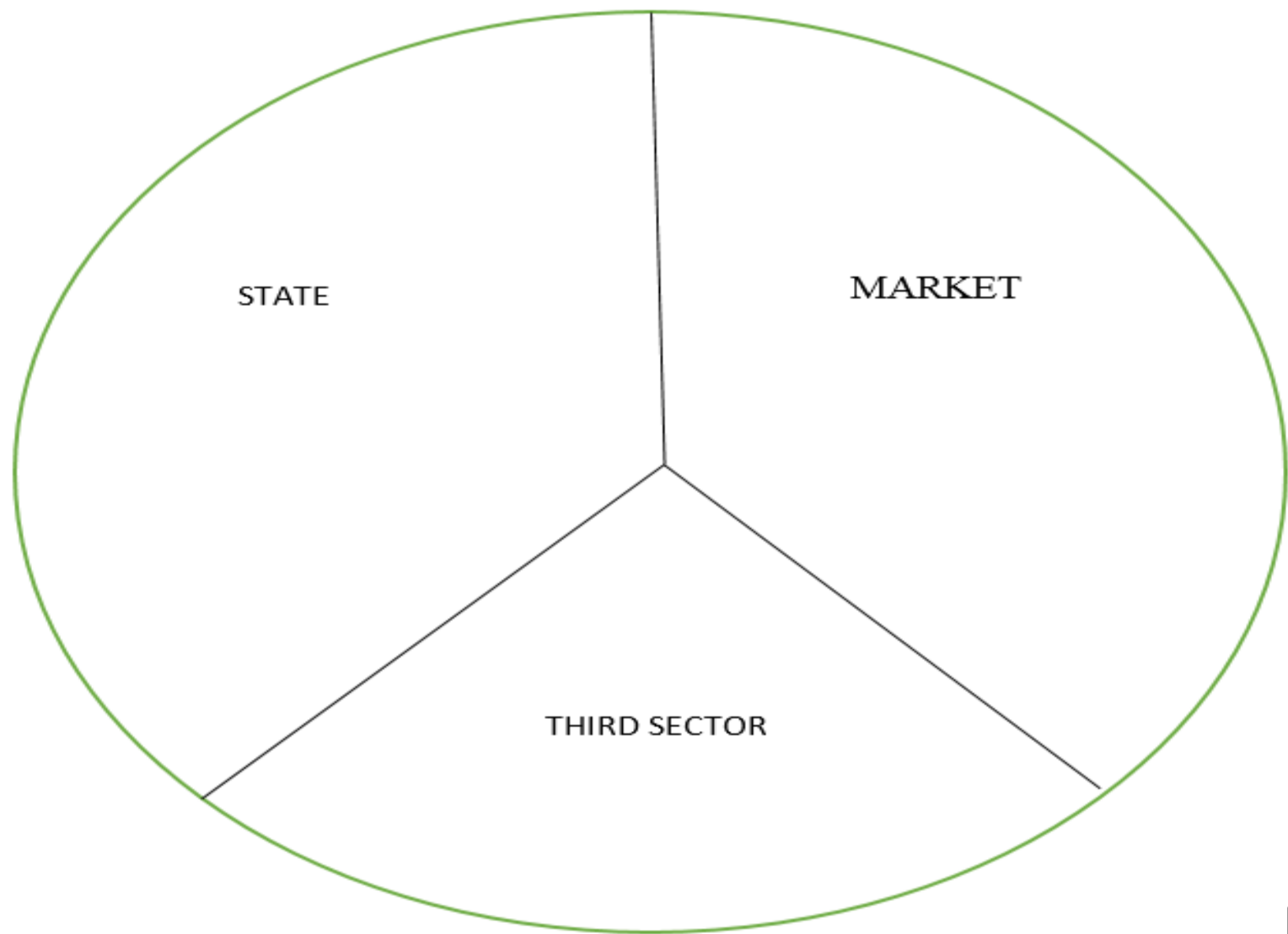
organised/institutionalised entities, which are private in nature (institutionally separated from the government), self-governed, non-profit distributing, and have some voluntary element in its management and operation.

# 3. Framing the Debates

## The American model

Conceptualises three formally organised sectors, as entirely independent of each other with their own characteristics, functions and motives in the economy;

- Public sector- redistributive role; redistributing income and wealth for the provision of public goods and services and other social welfare aims
- Private sector- acquisitive role; undertaking commercial activities for the purpose of income and wealth generation
- Non-profit sector- transfers/disposing income and wealth; voluntary and not for profit orientation with social objectives



# 3. Framing the Debates

## The American model

Creates a conceptual barrier for private-commercial entities to have social objectives which is the distinct domain of the non-profit/third sector and the public sector.

Fits perfectly with the separation of roles in the economy as argued by Ismail (2002)

# 3. Framing the Debates

The European model

Informal sector, e.g. families, neighbourhood communities and other non-formal groupings as an important source of social welfare- Welfare triangle

the seminal work of Esping-Andersen (1990)-

The Three Worlds of Welfare Capitalism

4 sources of well-being, 3 formal sector + informal sector of the households/families constitute the welfare diamond  
Conceptualised the third sector to be part of a welfare mix between the four potential providers of social welfare, where the third sector is located as an intermediate area rather than a clear-cut sector, often in the form of hybrids.



# 3. Framing the Debates

The European model

Recognises the potential overlaps between the structure, function and motive of various organisations, e.g. private-commercial entities who may share the social objectives of the third sector.

Commercial activities and social objectives are not mutually exclusive domains

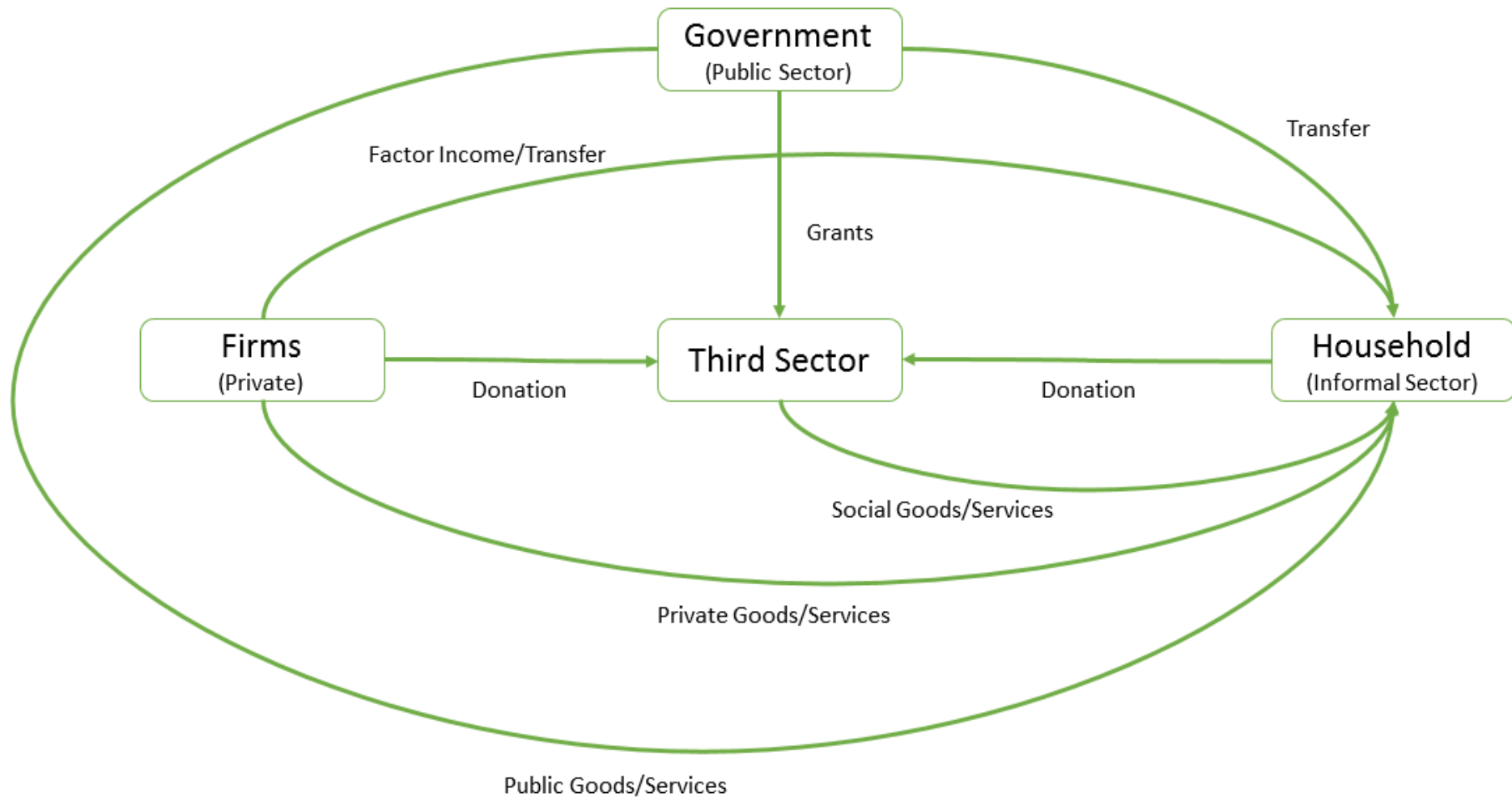
These hybrid entities are collectively known in the European literature as representing the 'social economy'.

This is in line with the Chapra model for IFIs.

## 4. An Integrated Framework of Social Welfare Provision

Uses a modified circular flow of income and expenditure model, as the basis for a framework that integrates the four sources of social welfare provision, i.e. the three formal sectors of private, public and third sectors, alongside the informal sector of the household. To locate the social responsibility role of IFIs within this framework.





# 5. Framing the SR Role of IFIs

Denial syndrome for SR role in the early stage of its emergence

3 important developments since then...

Increasing acceptance by the industry players on the SR role of IFIs.

The shift towards other potential institutions and instruments to promote socio-economic justice and well-being- revitalising zakat and waqf institutions

Other forms of commercial entities with social objectives - microfinance institutions, crowd-funding platforms, social enterprises, etc.

# 5. Framing the SR Role of IFIs

## Implications

The revitalisation of Islamic institutions such as zakat and waqf, and the proliferation of various forms of entities such as Islamic microfinance, socially oriented crowdfunding platforms, social enterprises and cooperatives has spread out the social welfare burden previously mounted primarily on the shoulder

- of Islamic financial institutions. This enables some essential role such as poverty eradication efforts, social protection, or micro-entrepreneurial development, which are not effectively addressed by IFIs being addressed by these other entities.

# 5. Framing the SR Role of IFIs

## Implications

The increasing awareness on the huge potential of third sector entities, particularly the institutions of zakat and waqf, in providing social goods/services left unfulfilled by the public and the private sectors, has stimulated serious efforts towards the systematic institutionalisation of them in the economy

- A responsible and people-centric government in the public sector, together with a strong family, neighbourhood and community spirit within the household sector, are also important sources of well-being

## 6. Conclusion

The integrated framework represents a macro model of a cooperative setting in which all sectors in the economy cooperatively contributing to the social well-being of the society without singling out any particular actor

This provides a proper framing of the SR role of IFIs in relation to the broader efforts towards realising socio-economic justice and well-being in the economy.

Provides a proper and reasonable context for social responsibility roles expected of IFIs.

***THANK YOU FOR YOUR  
KIND ATTENTION***