

## Exploring the Untapped Potentials of Islamic Social Funds in Islamic Home Financing for Low Income Family<sup>1</sup>

Akhmad Affandi Mahfudz  
Department of Islamic Banking and Finance  
Asian Institute of Banking, Finance and Informatic of PERBANAS  
Jalan Perbanas, Karet, Setiabudi Kuningan  
Jakarta 12940  
Telp: 525 2533 / 522 2501-4  
Fax: 522 8460 / 522 3064  
Email: akhmad.affandi@perbanas.id

### Abstract

Islamic home financing in Islamic financial institution hitherto remains an arduous to resolve as it contains many issues. One of the main issues is interest benchmarking that inseparable part of banking system. Amid this reality, many Islamic financial institutions ignored the existence of Islamic social funds to mobilize the funds and hence ameliorate the affordability of low income family to purchase a house. This paper therefore aims to explore the untapped potentials of Islamic social funds such as *waqf*, *Shodaqah* and *infaq* to mobilize funds and create more affordable house for low income families. This paper undertakes library review as qualitative approach to strengthen the discussion. This paper concludes that the synergy between *Nazir* of social funds and Islamic micro finance institution able to produce Islamic social funds to be utilized to help low income family afford to purchase a house. This paper implies practically on the expected remarkable growth of Islamic micro finance institution offering Islamic home financing using Islamic social funds approach.

**Keywords:** Islamic social funds, Islamic home financing, Islamic financial institution, Affordability, Interest benchmark

### Introduction

Finding an alternative rate for mortgage is not an easy way amid massive issues on Islamic home financing that practiced by Islamic financial institutions particularly Islamic banks. This sector is believed to contribute significantly and able to mobilize the funds that create multiplier effect of national economy. As significant pillar of national economy, home industry now becomes inseparable

---

<sup>1</sup> This research is funded by the Ministry of Higher Education under the Trans-Disciplinary Research Grant (TRGS)- SO Code: 13166

part of government policy that reacted with various issues such as economy, politic, social and culture. Therefore, it is no doubt that home ownership is the pulse of individual life and in fact, in Islam it is part of objective of Shariah (*Maqashid Shariah*) where muslims have to fulfill this objective.

The practice of Islamic home financing wrecks more challenges as it prohibits the use of interest as a benchmark. However, recent studies on Islamic home financing did not come to the expected rate that comply with the tenet of Shariah principles. In addition, removing interest benchmark indeed an arduous efforts that involve all stake holders including the government to come out with more Islamic rate, fairer and affordable price especially to low income families.

Amid this atmosphere, most of practitioners tend to ignore the significance role of Islamic social funds to create more affordable home for low income families. Islamic charity is always perceived as no impact to the economy and no significant contribution to ameliorate the purchasing power of low income families particularly to own the house. The existence of Islamic charity funds has no correlation with home financing that actually help the destitute to empower their household economy. Social fund is always regarded as for consumption purposes only.

Islamic social funds does not confine its understanding to merely describing as social gift that elapse with consumption of the recipient. Islamic social fund has distinct features of financing that empower low income family particularly to purchase the house. In this regard, financing for them with affordable repayment whilst empowering to penetrate high level of their productivity.

The concept of Islamic social funds is actually very close to social economy that associated with social justice. In many developing and least developed countries, social economy refers to a group of people undertaking some economic activity or entrepreneurship activity to enable them help eachothers when they encounter suffer and hardship.

Meanwhile the utilization of Islamic social funds has been proved to be the most effective way to eradicate social disease including poverty. At this juncture, home financing takes the role to reduce and eliminate the poverty through possessing the house. In order to materialize this, Islamic social funds and home financing should be merged and integrated with appropriate scheme of financing that comply with the tenet of Shariah principles.

It is therefore imperative to explore the untapped potential of Islamic social funds that help Islamic financial institutions to empower low income family to own the house.

### **Contribution of Classical Muslim Thinkers on Social Economy**

Classical thought on Islamic social economy has been deeply discussed among classical *muslim* thinkers. Al-Farabi stated that social fund is part of social economics and it is categorized as practical wisdom (*al-hikmah al-amaliyyah*)

that associated to conceptual wisdom (*al-hikmah al-nazariah*). Al-Farabi also mentioned that this conceptual wisdom comprises both ethics and knowledge of noble actions that produce human's behavior (Macarimbang, 2013 in Omar & Mahfudz, 2018).

Imam al-Ghazali, Al-Mawardi and Ibn Khaldun among the renowned scholars in their magnum opus who had great influence on the issue of social economy. For instance, Imam al-Ghazali who has great contribution on political economy, Ibn Khaldun who had devoted his formidable works on social group and muslim solidarity and al-Mawardi with his master piece of public finance. All these contributions aimed to achieve social justice, social welfare and social (Omar & Mahfudz, 2018).

### **Islamic Social Funds as Social Economy**

Islam is not merely religion, but its comprehensive way of life for human being. For instance, Islamic economics as part of Islam that regulated and solved to the materialistic philosophy of human's problems. Zakat and waqf are tool of Islamic social funds that contributed to social finance. Those instruments was proved in the history of Muslim's civilization.

Zakat is an instrument in Islam that guarantee fair distribution of income and wealth (Askari, Iqbal, & Mirakhor, 2014). This instrument (zakat) is a mandatory duty to Muslim's *ibadah* as it is part of Islamic principle. This appearance as core concept and tenets on the life of a Muslim, as reflected in these following verses:

*"And establish regular prayers and give the zakah and obey the Messenger so that you may receive mercy" (An Nur 24: 56)*

*"Truly those who believe and do righteousness and establish regular prayer and give the zakah, for them is their reward with their Lord. And there shall be no fear upon them neither shall they grieve." (Al Baqarah 2: 110)*

The Arabic words *zakat* means "purity" and "cleanliness", since giving away a part of one's wealth to the poor purifies his wealth as well as his heart, as Allah SWT says in the Quran verse below:

*"Take of their properties alms so that you may purify them and make them clean with it." (At Taubah 9: 103)*

According to Umar bin khattab (Auda, 2007,11), the higher intention of zakat in Islamic law (*maqasid al-shariah*) is a form of social economy that is paid by the rich people for assisting the poor people. In summary, *zakah* can be able as a method for economic growth and stabilization by eliminating the huge gap between the rich and the poor. The rich people gives financial help by way of food, clothes and shelter to the poor and needy; gives financial help to those who are in debt. It enables them to pay up their debts; gives a preventive measure against criminal actions that the poor may be forced to take in order to survive.

The waqf institution is the fundamental philanthropy charity in Islam, its forms an integral part of the Islamic way of life. Charity in Islamic views as not only wealth transfer from rich people to the needy, but as a mechanism for self-development and community for achieving Allah's approval and reward in this world and the Hereafter.

*Waqf* derived from the Arabic language as *Waqafa*. *Awqaf* is the plural of *Waqf*. The *Waqf's* concept is used in Islam to explain definite property that acquired by people and preserved for the restrained benefit of any philanthropy used (Karim, 2012). The concept of *Waqf* was developed by the Holy Prophet Muhammad SAW and since then it has played a vital role in fulfilling the needs of Islamic civilization.

Mohsin et al., (2016) classified waqf into two types, according to al-mawquf 'alaih (the beneficiaries) and al-mawquf (endowed property). First category can be divided into three types which are:

1. Waqf khayri (public waqf), an endowment made by the founder to support the general good and welfare of the poor and the needy in society.
2. Waqf ahl (family waqf), the founder endows his property to his children and grandchildren, relatives or to other persons he specifies.
3. Waqf mushtarak (combined public and family waqf), to support both the public and family.

Moreover, for second category can be classified also into 3 types as follow:

1. Immovable and movable property, the immovable includes lands, fields, farms, or buildings meanwhile the movable can be in form of money that we know as cash waqf.
2. Sound and unsound waqf, privately owned or state owned property.
3. Direct and indirect waqf, direct waqf created to serve the people free of charge whereby the creation of indirect waqf is needed in order to provide expenses for those direct waqf.

Once a property is created as *waqf*, there are restrictions for this object which are irrevocability (the founder can't change its status), perpetually (to ensure regular and continuity to financing needy areas), inalienability (it can't be subject of any sale, disposition, mortgage, gift, inheritance, or any alienation). The purpose of this instrument is not for the sake of profit but to contribute to the welfare of society and seeking compound rewards in the hereafter (Mohsin, 2013)

During the time of Ottoman Empire, waqf property is an instrument to assist the needy people for housing. The waqf property based on *ijarah*, which limited tenure. This waqf also called *icare-i tavile*, which means the long term renting of an endowment property became possible for the first time (Cizakca, 2004).

The way forward to efficiently run institution of *waqf* to contributed human welfare by distributed equality among the people can be achieve through but not limited to these following steps:

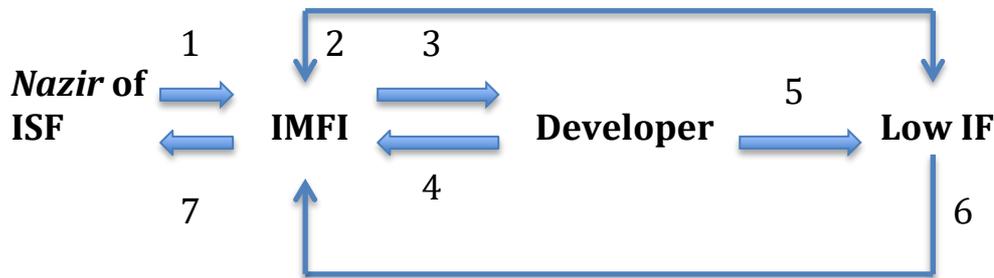
1. Increase participation, the on-going success of these institutions for centuries has only been possible due to the small continued donations made by immense number of ordinary people enlightened in the spirit of Islamic charity. Therefore, emphasizing on non-property *waqf*, like cash *waqf*, can be maximize opportunity for those who are not in possession of real property to participate in *waqf* endowment.
2. Proper utilization, efficient collection, distribution and distribution in productive usage are important factors to achieve, as establishment of the system that can measures performance of each institution, will lead to big impact for long term purpose in the society.
3. Management reform, mismanagement can destroy all the function of the institution, therefore whether the non-profit organization or the government should manage *zakah* and *waqf* institutions professionally.

### **Islamic Social Funds and Islamic Home Financing**

There might be a question on how Islamic social charity can mobilize the funds and relate to Islamic home financing. In Islam, owning the house is part of fulfilling *Maqashid Shariah* where one has to undertake shelter to protect individual right of survival. In addition, the understanding of having house confines for the sake of survival and for productivity purposes. In this regard, low-income family has the right to receive the designated property (social funds). However, as of now, most of financiers ignored how to help the poor owning the house. Most of financiers focusing on the product that wreak benefit rather than social contribution. In addition, the collection and disbursement of this charity remain modest and far from the expectation. As result, house ownership remains sluggish growth particularly among developing countries and least developed countries where poverty remain an arduous to combat.

According to previous studies, Islamic financial institution particularly Islamic bank is not the appropriate institution to offer Islamic home financing for low income family (poor). The offered rate by Islamic banks particularly using *Musyarakah Mutanaqishah* found not to be feasible. It can be implemented through Islamic micro finance institution like cooperative or *Baitul Maal Wa Tamwil* as an investment avenue to address the social well being of its members (Meera & Razak, 2009).

Islamic social funds shall not be perceived as mere consumption for the recipients. As home is their basic need, the social funds need to be utilized to



**Note:**

- ISF = Islamic Social Funds
- IMFI = Islamic Micro Finance Institution
- Low IF = Low Income Family

empower them and afford to buy the house. The following diagram depicts this scenario where Islamic social funds along with Islamic micro finance institution can work together to help the low income family to own the house.

As common practice, Islamic social funds like *zakat*, *waqf* and *infaq* are managed by professional *Nazir*. In this regard, Nazir will deliver the ISF to IMFI. The fund that received by IMFI will be used to reduce the price of house given to low IF. On another note, IMFI at the same time will select the eligible recipient from low IF to receive financing and generate income to pay the installment. Selection of low IF have to undergo rigorous process with strict appraisal to avoid default risk. In this case, IMFI have selected the right recipient from low IF prior to extending funds from Nazir of ISF to IMFI. However, in the event of default payment, IMFI would value the collateral (house). Any profit and loss will be shared according to the principle and spirit of *Musyarakah Mutanaqishah* contract. To mitigate any risk, the financing will be secured by financing scheme using modified Islamic Grameen model. The practice of modified Islamic Grameen model for the poor has been recorded to be successful with almost zero NPF (non performing financing). At this juncture, IMFI will always make sure that the recipient of financing able to pay the installment of the house. Therefore, IMFI has the obligation to coach and guide Low IF to run their entrepreneurship activity to generate income and profit. At the end, Low IF would be able to pay two installment namely house installment and working capital installment.

**Conclusion**

Based on classical thought by muslim thinkers on social economy, social funds is part of social finance to establish social justice as part of *Maqashid al-Shariah*. Meanwhile, the implementation of Islamic home financing for low income family indeed the best solution amid unresolved issues in Islamic financial institutions.

It is imperative to undertake formidable efforts by all stake holders to execute this as the success of home ownership for low income family would generate multiplier effect to boost national economy.

On another note, there must be good literacy among muslim that Islamic social fund is the best solution to mobilize the fund that empower the destitute particularly to own the house. Nazir of this fund should undertake this as public trust in managing the fund while Islamic micro finance institution have to ensure that no doubt on the success implementation of utilizing Islamic social funds to help low income family to own the house.

## References

Askari, H., Iqbal, Z., & Mirakhor, A. (2014). *Challenges in Economic and Financial Policy Formulation An Islamic Perspective* (first edit). New York: PALGRAVE MACMILLAN.

Auda, J. (2007). *Maqasid al-shariah as Philosophy of Islamic Law A Systems Approach*. The international institute of islamic thought london.

Aydin, Necati. (2015),"Islamic social business for sustainable development and subjective wellbeing", *International Journal of Islamic and Middle Eastern Finance and Management*, Vol. 8, Iss 4 pp. 491 - 507

Affandi, A. & Astuti, P. (2013). An Analysis on the Dynamic Model of Ibn Khaldun on Poverty in Majority and Minority Muslim Population", *Humanomic: International Journal of Sytem and Ethics*, Emerald Group Publishing, Vol. 29, No.2, 2013 pp 136-160 ISSN: 0828-8666

Cizakca, M. (2004). Ottoman Cash Waqfs Revisited : The Case of Bursa 1555-1823. *Foundation for Science Technology and Civilization*, 1-20. Retrieved from <http://www.fstc.co.uk>.

Ismail Abdel Mohsin, M. (2013). Financing through cash-waqf: a revitalization to finance different needs. *International Journal of Islamic and Middle Eastern Finance and Management*, 6(4), 304-321. <http://doi.org/10.1108/IMEFM-08-2013-0094>

Karim, R. (2012). Zakat and Waqf Bank - For Social Development and improved Management of Endowments. *International Waqf Conference*.

Lung, L. C. (2014). Musharakah mutanaqisah partnership in Malaysia's Islamic bank: a comparison between theory and practice. *American Journal of Economics and Business Administration*, 5(3), 95.

Macarimbang, A. To. (2013). Envisioning a Perfect City: An Introduction to Al-Farabi's Political Philosophy. *Journal for Islamic Identities and Dialogue in Southeast Asia*, 1, 73–92

Meera, A. K. M. & Abdul Razak, D. (2009). Home financing through the musharakah mutanaqisah contracts: some practical issues. *Islamic Economics*, 22(1).

Mohsin, Hisham, M. I. A., Cizakca, M., Alhabshi, S. O., Shaikh Hamzah Abdul Razak Seyed Kazem Sadr, Thamina Anwar, & Obaidullah, M. (2016). *Financing The Development of Old Waqf Properties*. (M. I. A. Mohsin, Ed.).

Omar, Azmi. & Mahfudz, Akhmad Affandi. (2018). *Islamic Economics Text Book*, International Shariah Research Academy for Islamic Finance, Forthcoming Publication.