ISLAMIC WEALTH MANAGEMENT IN HISTORY AND PRESENT

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When contemporary Islamic economists

discuss Wealth Management,

they understand accumulation of wealth **and** its redistribution

within an Islamic framework.

In my paper, I will also follow this method and

discuss first the accumulation of wealth and then its redistribution.

But my paper will differ from theirs in that

my approach will be historical and will cover

from the birth of Islam in the 7th century to the present.

It will also differ from them in that

I will focus on the institutions and their evolution,

While in this way I will combine

Macro and micro economic dimensions,

they focus on the micro primarily to

service high net-worth individuals in

Saudi Arabia and the Gulf.

Accumulation of Wealth in Islam:

I have argued elsewhere[1] that

the classical Islamic economic system was capitalistic.

[1] Murat Çizakça, *Islamic Capitalism and Finance, Origins, Evolution and the Future* (Cheltenham: Elgar, 2011).

But, this was an ethical, commercial and pre-industrial capitalism.

Evidence:

The evidence for this argument can be found

in the classical sources of Islam: i.e., The Qur'an, the prophetic traditions and the verdicts of the major jurists.

Principles:

From these sources we deduce the following economic principles

for capital accumulation

a) Competitive markets
b) No upper limit to profits providing they are *halal*
c) No interference in prices
d) Modest taxes on trade
e) Interest Prohibition

But principles are in theory.

They need to be translated into practice by institutions.

Institutions:

Classical Muslim jurists deduced the following institutions from these principles:

a) Institution of *Ihtisab* controlling the markets and ensuring competition
b) Free trade given utmost priority. The most advanced maritime law of the middle ages was developed by Muslims. This law was then taken to Europe by Eleanor of Aquitaine and her son Richard the Lion Heart of England. This was the beginning of the Lex Mercatoria in medieval Europe.
c) Interest prohibition could only be implemented if the capitalist and the entrepreneur could be linked, by an alternative non-usurious method. *Mudaraba* partnership was the solution. This partnership and its derivatives were also borrowed by the Europeans, particularly the Genoese and the Venetians, and were incorporated into the *Lex Mercatoria.*

d) The *raison d'etre* for the interest prohibition and its substitution with business partnerships was to ensure risk sharing. But risk sharing leads to profit and loss sharing as well. The overall result is a share economy. This was the essence of the classical Islamic economy, or the capital accumulation segment of historical Islamic wealth management.
e) All of these institutions were enhanced by the annual pilgrimage, which brought together in Mecca merchants from all over the Islamic world and united the Mediterranean and the Indian Ocean world economies. Muslims controlled this link between the two world-economies for about a millennium from the 7^{th} century to the 17^{th}.

It was these principles and the institutional set up which,

created the massive wealth of the Islamic world in medieval period.

Capital Re-distribution:

a) Taxation

Every society needs to redistribute the accumulated capital in the economy.

In Western economies the usual venue for this is taxation.

But in Islam, taxation is paradoxical, because,

it is considered as an infringement of

one of the most important purposes of the Islamic law–

protection of wealth.

On the other hand, it is essential for defence.

The Qur'an mentions only three taxes by name.

These are*, zakat, kharaj and jizya.*

The first one was due to the Muslims and was applied at 2.5%.

In agriculture it could go up to 10%, or even more, depending upon the local conditions.

The other two were due to the non-Muslims, who paid higher rates, because

they were exempt from military service.

Over all, the tax burden in the classical period was negligible.

This has raised the issue of how to finance the state expenditure.

Modern Islamic economists have argued whether it is possible to

add additional taxes to the Qur'anic taxes.

It is generally agreed that this would be legitimate,

only if the country is under enemy attack.

This also implies that any tax revenue must,

first of all, be spent for defence.

This is confirmed by the 1527 budget of the Ottoman state.

This budget reveals that bulk of the state expenditure was

allocated to the military.

The Ottoman state spent hardly any money on

Such vital services as health and education.

Waqfs:

It was the waqf system which financed, set up and maintained

schools, hospitals and all the other civilian needs.

How do we explain this?

Waqf emerged in the Islamic world in response to a

Statement of Prophet Mohammad.

The statement was simply this:

"When a person dies, all his/her acts come to an end except three: useful knowledge, continuous charity and a pious offspring".

Thus, Muslims established waqfs essentially with a religious motive,

to save their souls in the hereafter.

A waqf combines all these three acts and

allows a person to have his/her sins eventually forgiven by

obtaining good deeds.

Muslims believe that they can do so by

donating their properties to a charitable purpose and then

channelizing the usufruct generated to this purpose.

At this point,

I would like to explain the modus operandi of a waqf

by answering the 10 questions of Prof. Toru Miura so as to facilitate cross-cultural comparison.

1) **Who are the donors?** Anyone who had the means. But the military class was predominant.
2) **What is donated?** Until the 15th century, real estate, both rural and urban. Cash began to be donated during the 15th century and increasingly became popular. After the year 1908, waqfs could also be established with joint-stock company shares.
3) **Who receives the donation?** A donation could be self-standing or attached to another waqf. Usually, a large donation contained its own mosque, bazaar, school, public kitchen and even a college. This was the so-called waqf kulliyah, or a complete waqf. Individuals with lesser means could contribute to an already existing waqf. When a complete waqf was established, myriad of people benefited: people who prayed in the new mosque, merchants and craftsmen who practiced their trade in the bazaar, the poor who could eat in the kitchen and the students who studied in the college.
4) **For what?** Purpose was primarily religious. But eventually, the military class, whose property rights were in jeopardy, began to donate their properties in the form of waqfs and appointed themselves and then their

offspring as trustees. The motive thus became, in addition to religion, also to protect the property from confiscation. Still another motive was to side step the Islamic law of inheritance. Founders, who wanted to transmit their properties to the most trustworthy offspring , used the waqf for this purpose.

5) **Who owned the donated properties?** Allah!
6) **Who managed the donated properties and how were they managed?** Usually, the donors appointed themselves as the initial managers. Then the management was to be entrusted to the most capable and trusted offspring. Finally, rules were laid down by the founders how to appoint trustees after the family became extinct. When this happened, courts or in the 19th and 20th centuries Turkey, centralized Directorates of Waqfs (DoW) appointed suitable trustees. Waqf accounts were annually inspected either by the courts or by the DoWs. In Malaysia, SIRCs are the sole trustees of all the waqfs in a state.
7) **For what was the income used?** The usual purposes were those mentioned in the statement of the Prophet. But many other purposes eventually emerged. This was independent, decentralized decision making in response to local needs.
8) **Did the state tax the donated properties?** Cash waqfs were tax exempt. Because they were considered to have been established with already taxed income (after tax income). In rural areas, there were no uniform rules. Taxability depended on the status of the land donated.
9) **Deeds of Donation.** A *waqfnameh,* informs us who the founder was and with what purpose the waqf was founded and in what year. It then informs us about the extent and nature of the *corpus.* We are then informed how the annual revenue is to be spent. Another source is the cash waqf annual inspection registers kept by the Shari'ah courts. These inform us about the amount of cash that was endowed, to whom it was lent and at what percent, the total annual return this cash generated and the purpose for which it was spent. These records are very well preserved and can be found in Turkey among the so-called *Şer'i Mahkeme Sicilleri.*They also exist in major Arab cities.
10) **What kind of social relationship is organized by the donation? Corporate body, personal network etc?** Notwithstanding the arguments of some orientalist authors, a waqf, at least during the Ottoman era, possessed judicial personality. This is proven by the fact that the so-

> called *marsad* waqfs could borrow money in their own name, not in the name of their founders or the trustees. A waqf was also a quasi corporate organization in that it had its own life separate from its founder or the trustees. Consequently, waqfs enjoyed longevity. The reason why they are not considered as fully incorporated is that they did not provide owner and entity shielding.

To sum up,

waqf was the most important institution in the Islamic world to build up human capital.

It was not, however, unique to the

Islamic world as other cultures, particularly Japan and China,

developed their own similar systems.

In the West, however,

European foundations and trusts were

borrowed from the Islamic world when the

crusaders “visited” the region.

It has been shown that Merton College of Oxford

as well as Peter’s College of Cambridge were

designed originally as waqf institutions.[2]

The borrowing did not stop with Oxford and Cambridge and

spread to the United States as well.

Today, nearly all the top US universities have

either been established as trusts or

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[2] Monica Gaudiosi, “The Influence of the Islamic Law of Waqf on the Development of Trust in England: the Case of Merton College”, *University of Pennsylvania Law Review*, vol. 136, no. 4, 1988.

have their own trusts/foundations.

Decline of the Islamic Capitalism

It goes without saying that

Islamic world today has some of the poorest

countries in the world.

This stands in sharp contrast to the period 7th-13th centuries when

it was one of the most advanced civilizations in the world.

What went wrong? When did the decline start?

These are difficult questions.

I can only answer them with a hypothesis.

During the period 11th-13th centuries,

Islamic world suffered a pincer attack:

From the West the crusaders and from the East the Mongols.

These attacks were so fierce that the

very survival of Islam was at stake.

Defense needed powerful, centralized states

that could mobilize the population.

Heavy taxation to finance huge military build up was needed.

All of this was achieved and

both invaders were eventually expelled.

It was the Turkic states who achieved this.

But this occurred at the huge cost of substituting the liberal, classical Islamic capitalism with

the proto quasi-socialist states.

Defence was achieved, Islam was saved but

economy was socialized.

Spice trade came to be monopolized by the Mamluks.

State interference in the economy increased in time.

Ottoman economy constituted the pinnacle of the

proto quasi-socialism.

These developments coincided with the rise of

Western capitalism which,

culminated with the industrial revolution.

As a result,

all three Islamic empires,

the Mughal, the Safevid and finally the Ottoman empires

succumbed to western capitalism.

Attempts of Recovery

Bulk of the Islamic countries regained their independence

after the second world war.

This was an exciting period and

Muslims wanted to re-design their

economies according to Islamic principles.

They felt this need because

they knew that the prevailing economic system in their countries was imposed by western imperial powers.

They also knew that,

this system was designed for the *homo-economicus*.

But they claimed that *homo-Islamicus*

is a different species and needs a different

economic system.

They felt, the easiest point to start had to be the financial system.

This meant, primarily, a new interest free

financial system.

The very first Islamic bank was established by

Dr. Ahmad al-Naggar of Egypt in 1963.

Dr. Al-Naggar did this by modernizing the

Classical *mudaraba* partnership.

This was 100% in conformity with the

Classical Islamic law (a pure profit and loss sharing system)

was initially a great success.

Before long,

many other Islamic banks were established.

But, there was a huge shortage of personnel

trained in correct Islamic finance.

So, the industry came to be invaded by

conventional bankers.

Today, Islamic finance is dominated by the

Shari'ah compliant mode.

It works like this:

Islamic bankers take conventional financial instruments,

then they reverse engineer them to make them

“Shari’ah compliant”.

Then they claim that they have a new “Islamic” instrument,

whereas what they have done is actually to put an

Islamic cloak upon a conventional instrument.

This is the “Shari’ah compliant” approach.

This is now completely discredited among the academia.

I have argued elsewhere that

a better approach would be the Shari’ah based approach.

This involves modernizing genuine Islamic institutions.

Al-Naggar’s was a good start.

Another example is the Tabung Haji of Malaysia.

Established by Ungku Aziz,

Tabung Haji modernized the preparation for

the ancient tradition of pilgrimage.

Still another example might be the

modernization of the Ottoman public borrowing

instrument of “esham”.

Finally,

we can also mention the evolution of waqf of stocks

from the classical Ottoman cash waqfs.

Conclusion

I have tried to explain Islamic wealth management
from a historical and institutional perspective.
On the capital accumulation side,
today, there is a great struggle to
protect the system from the invasion of conventional finance.
This is also a struggle between
risk sharing and risk shifting.

On the capital re-distribution side,
there is also a struggle to modernize
the waqf system.

In short,
Islamic world is desperately searching for an
economic model that is not only in
conformity with its principles and traditions
but also able to address the demands of the contemporary world.