

DECENTRALIZED ASSETS, BANK FAILURES, AND GREEN FINANCE: TIME FOR A SHARIAH-COMPLIANT MONETARY SYSTEM?

The Centre for Islamic and Middle
Eastern Law (CIMEL) at SOAS presents:
SOAS-QFC Workshop on Islamic Finance

Program of Events

TIME / DATE / LOCATION

08:30 - 17:00, Thursday, 15 June 2023

Brunei Gallery (BG01-02)

SOAS, University of London, 10 Thornhaugh Street, London WC1H 0XG

OVERVIEW

This year, the 18th (since 2006) annual workshop on Islamic finance, we are again proud to be back and to be hosted once again by the School of African & Oriental Studies (SOAS) at the University of London. At SOAS, being the 5th in the annual series at this university, we are very fortunate to be aligned with enthusiastic and talented individuals in the field, led by Dr. Jonathan Ercanbrack, Chair, Centre of Islamic and Middle Eastern Law, SOAS.

In the last workshop in 2022, participants discussed *Cryptos: Distinguishing Hype from Realities in Islamic Finance*. To continue to enhance the ongoing discussions between Islamic economists, practitioners, lawyers and *Shari'ah* experts and scholars, this year participants chose to focus the 2023 SOAS Workshop around the topic of “Decentralized Assets, Bank Failures, and Green Finance – Time for a Shari'ah Compliant Monetary System?”, the most preferred option selected by our participants.

Within this context, the initial focus of the workshop will be through use of a short presentation by a representative member of the central bank of the United Kingdom (the Bank of England) on its emerging interest in Islamic finance as well as on its initiatives for an alternative liquidity facility, all to better understand the current stability of the incumbent fractional reserve monetary model. The purpose is to review and to reassess the current monetary system in the context of *Shari'ah* compliance. It also aims to see how and when *Shari'ah* compliant financial products can be used with or rather alone from the incumbent system, or even be ‘enhanced’ by new technologies and ESG initiatives, such as Green Finance, that are stretching our traditional methods of fiat global currencies.

As with prior similar events, participants come to the Workshop having sent their comments on the topic in advance. This allows participants to start the Workshop at an advanced stage and to maximize the use of the workshop time. A detailed program of events is prepared from the participants’ comments. Therefore, participants are kindly requested to have read in advance all of the circulated papers and comments, as they become the basis of most of the day long discussions on the Workshop theme.

Running for 18 years now, this is a unique annual event with little parallel in the Islamic finance industry. This series of annual workshops along for a select group of established *Shari'ah* scholars, economists, legal luminaries, bankers and top industry professionals gather for a day long close-door discussion on an important contemporary theme within the field of Islamic finance, as pre-selected by these top decision makers in the industry.

INTRODUCTION

This year, participants are encouraged to discuss and evaluate whether the conditions have been met to consider adopting a separate monetary system within the realm of Islamic finance, either for a specific test-case nation like Malaysia or across multiple jurisdictions.

Since the last workshop in June 2022, the world has witnessed significant financial challenges, from rampant inflation (prompting a series of interventionist rate hikes), to certain bank failures not seen since the financial crisis of 2008, to geopolitical tensions which are leading to a redraft of international financial rules and trade flows, to further breaches of national debt ceilings, to an increase in bank NPLs, to great volatility, scandals and serious regulatory scrutiny of crypto currencies, to a widening of economic disparities between those who have and those who do not, to the economic effects of unprecedented ecological and natural disasters, and to real challenges to the hegemony of the US Dollar as the world's base currency. At the same time, the world has seen further developments, enhancements, and opportunities, in the fields of decentralized finance (deFi), blockchain technologies, other forms of cryptocurrencies, CBDCs, and even the development of Green sukuk / Green bonds and other ESG related financial products.

Collectively, all these universal challenges as well as new entrants to the global field of finance can prompt some new and interesting opportunities as well as bring in some new thinking to the field of Islamic finance. Of which, participants are encouraged to assess the merits of whether or not these current events have opened up a new unique window of opportunity to create a separate or even hybrid form of monetary system for Islamic assets, either on an individual national test case, or even more optimistically, across multiple jurisdictions. If there is a sufficient merit or argument in favor of doing so, participants are asked realistically how this can be achieved. Furthermore, what else needs to be carried out to turn this into a reality.

Within this backdrop, workshop participants are encouraged to reflect on whether this initiative is even applicable in other countries other than Malaysia? Is this even desirable or wanted? As Islamic financial institutions struggle to gain significant market share in a greater regulated and complex current business environment, should they have to be weighed down even further with even more new regulations and stricter *Shari'ah*-compliance standards? Will initiatives like green finance and deFi help address the arguably widespread skepticism concerning the *Shari'ah* authenticity of Islamic financial products? How can concerns regarding current *Shari'ah* compliance of Islamic financial products be better managed with now additional separation and standards? Is the *Maslahah* of creating further confidence in an emerging, growing industry more important?

Below are some initial questions that this year's workshop hopes to examine. We rely on you, the participants, to help us to develop these ideas and to consider ones which we have not addressed.

We also encourage participants to look deeper into the meaning of compliance and certification. Is *Shari'ah* compliance a matter not only of adhering to the basic rules of *fiqh* on contractual structure, but also a matter of adhering to principles such as those of the *maqāsid al-Shari'ah* as defined by consensus of the public and current public sentiments and values? Islamic finance is frequently required to choose between the application and enforcement of *Shari'ah* legal principles (as currently understood and applied), or, to justify new exceptions, all in order to overcome contemporary regulatory, compliance, credit risks, investor appetite, and market financial

challenges. So how can *Sharī'ah* scholars have the freedom to amend or revoke their advice with new developments/thinking, without subjecting their prior decisions to critical review?

This workshop is not meant to be a review of all forms of contemporary *Sharī'ah compliant* products and processes, but rather focused on the *Sharī'ah* challenges Islamic finance must address to ensure their compliance. Therefore, the main purpose of this workshop is to go back to the original unresolved debate on whether to use and apply the *akham fiqhiyya*, and/or, *hiyal*, *makharij* or other exception based Islamic principles, to achieve a specific *masalah* or *masalih*, within a contemporary financial strategy.

This day long roundtable workshop also aims to foster dialogue among the diverse professions represented by the participants, and to initiate collaborative efforts in solving some of the most urgent unresolved challenges in enhancing Islamic finance.

In order to maximize the benefit of this workshop for all participants, workshop attendees are kindly requested to avoid some of the repetitive discussions tackled in previous workshops, but rather to focus more on specifics to enhance the level of discussions above, and to hopefully bring out new or non-discussed sub-issues, and/or to agree on a realistic way forward.

OBJECTIVES

In this workshop, we would like to examine the workshop theme from the following angles:

- *Sharī'ah Social Ideals* – How can the *Sharī'ah* remain rooted to its idealistic economic goals (of social justice, fairness, wealth distribution, profit & loss sharing focus, etc.), whilst being able to adapt and remain relevant in a highly competitive modern financial world.
- *Maslahah Determination* – As with all of our workshops, continue to discuss how can we continue to apply *maqāṣid al-Sharī'ah* and agree on the 'ideal' *maslahah* for new Islamic financial products, especially those that challenge existing structures and methods? How to determine and deal with disagreements on *maslahah*? Should a "*maqasidic* or ethical index" be developed for Islamic financial products?
- *Sharī'ah Compliance* - Should *Sharī'ah*-compliance mean a financial product is compliant with the principles of the *Sharī'ah*, or rather, compliant with the strict interpretation of the rules (*ahkam*) and of the fiqh. In other words, should it be more principle based, or rather, factual rule based, or other?
- *Challenging Certification* - To understand on what basis and when can fatwa be 'enhanced', amended or disregarded by 'globally accepted standards' such as SDGs and green finance / green sukuk, once issued on Islamic financial products. How we can create certainty in the market if such opinions can be challenged, amended or recalled? Should there be different levels, standards or forms of compliance?
- *Sharī'ah Authenticity* – How do we maintain the authenticity of Islamic financial products if they are prone to non-standardization and frequent or unexpected change due to varied opinions?
- *Value Proposition and Distinctiveness* - What is the value proposition of *Sharī'ah* Compliant financial products, especially if they are open to new variant views and interpretation? What is fixed and what principles are open to interpretation? How can the industry maintain the distinctiveness of Islamic finance?
- *Qualification* - Who is qualified to challenge and on what basis can such objections be raised. Should it be left to specific, learned individuals, or rather, open to the public to challenge, or both. Is a proper method to make such a challenge (i.e., open public criticism, review board, escalation, or other?)

WORKSHOP AGENDA

8:30 a.m.	Reception and Coffee
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9:00 a.m. Welcome Remarks by Dr Syed Nazim Ali

9:05 a.m. Opening Remarks on behalf of SOAS, Dr. Jonathan Ercanbrack

9:10 a.m. Introduction by Workshop Moderator, Professor Volker Nienhaus

Part 1: Monetary Systems: Debt-based Money and Islamic Finance: Friends or Foes?

9:20 a.m. **Presentation:** A quick overview of the conventional monetary system from the perspective of a Bank of England representative, Mr. Arshadur Rahman, along with their alternative liquidity facility and how this relates to *Shari'ah* Compliance as a focus.

9:30 a.m. **Participants' Views – Open Floor Discussion**

Opportunity for each participant to explain briefly their views on the following. Do you agree/disagree with the following statements and questions?

With increased bank failures, rampant inflation, greater financial volatility (including for Cryptos), increased debt burden, widening economic gaps, increased geopolitics [rewriting international trade & finance], and general financial instability.¹

1. Can Islamic finance continue to develop and thrive strictly within the confines of a fractional reserve model?
 2. Is there a sufficient case to argue for a compliant monetary system to govern Islamic assets? Is it needed? Will it help?
- *Are these challenges an indicative need for a new or alternative Monetary System for Islamic Finance – or – Should Islamic Finance Continue to Work on Improving the Current Model?*
 - *Is it even possible to exist outside of the fractional reserve banking model? Is it feasible? Is it even desirable for a full break from it?*
 - *Are these Shari'ah challenges, or rather, mere economic, financial and political policy reasons?*

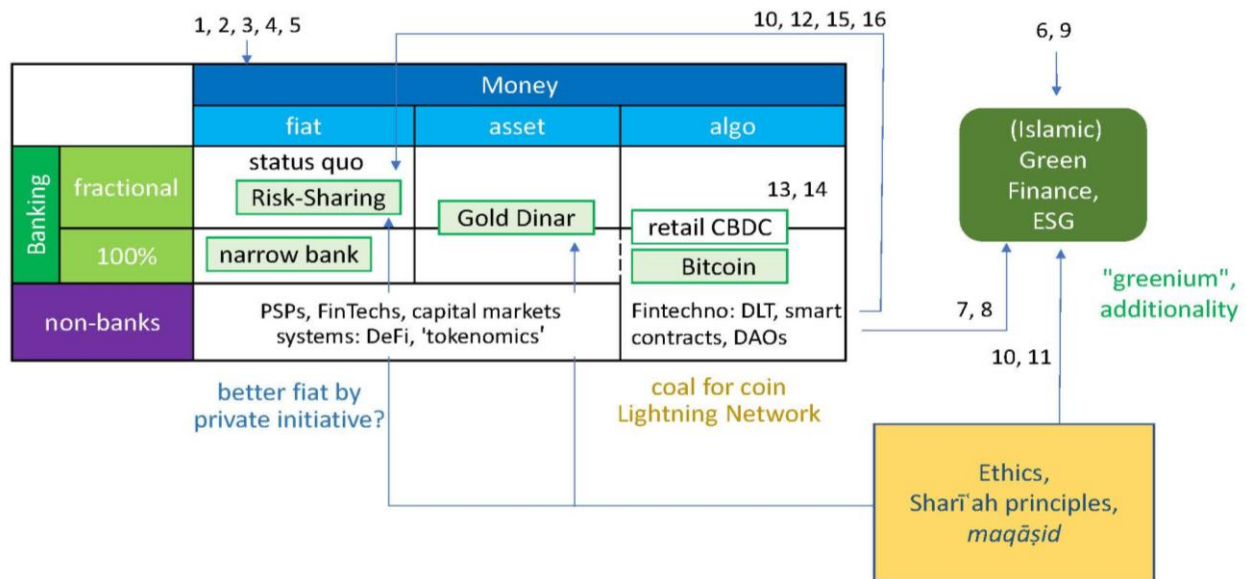
¹ The sequence and order numbering of these questions are placed intentionally as per Table 2.

3. Are there any aspects of a monetary system that need to be adjusted when Islamic finance assets are more than 50%, as in Malaysia?
- *Time to ditch the Green-Back for another asset class? Or all just wishful thinking?*
4. If it is not ready, what is still needed in order to create a unified national or global monetary system that serves Sharī'ah compliance?
- *If you say Islamic Finance is still far too small to go it alone nor to be able to influence the incumbent system, then realistically how 'big' does it have to become before it can do so? Can we put actual numerical & size targets?*
 - *What about aligning with other existing models, such as narrow banking?*
5. If ready, what needs to happen to make it a reality?
- *Who is responsible?*
 - *What can Central Banks and regulators (like some of those invited today) do to move this forward?*
 - *Are Malaysia's / [Indonesia's] monetary plans arguably a catalyst?*
- Other relevant considerations:
- *Sharī'ah compliant money in history and perspective (including gold/commodities/cryptos).*
 - *Booms, busts, redistribution: system or policy failure?*

Table 1:

		Money		
		fiat	asset backed	algorithmic
Banking	fractional reserves (debt created bank money)	status quo (inflation, redistribution bottom-up, recurring banking crises, short-termism, neglect of social returns) Risk-Sharing	commodity monies, classical Gold Standard Gold Dinar	monetary policy rules (e.g. k-percent, inflation targeting, Nash's ICPI) retail CBDC
	100% reserve (lending based on deposits)	Chicago Plan (1933, 2012 revisited), narrow banking , Mervyn King, Full Money Movement (Swiss)	gold/silver coinage, six Islamic money commodities	Bitcoin (PoW vs. PoS) asset-backed crypto money
non-banks		PSPs, FinTechs, capital markets systems: DeFi, 'tokenomics'		crypto currencies crypto assets/tokens Fintechno: DLT, smart contracts, DAOs

Table 2:



11:05 a.m. Summary – Moderator to provide a summary of all the points of view and frame questions. (10 mins.)

11:15 a.m. - 11:30 a.m. Tea/Coffee Break

Part 2: Fintechonology: What, Where, & Why in Islamic Finance?

11:30 a.m. Participants' Views – Open Floor Discussion

Opportunity for each participant to explain briefly their views on the following considerations on decentralized assets and fintechonology's applicability to Islamic finance and *Sharī'ah* Compliance. Do you agree/disagree with the following questions and statements?

12. DeFi (Decentralized Finance) Phenomenon: A Challenge or rather an opportunity for Islamic Finance?²

- *From a Sharī'ah perspective, is decentralization of finance a 'good' thing or even 'desirable' given the historical emphasis of centralization and/or the role of the state in Islam (e.g., zakat, jizya, rabb al-mal, etc), or not?*
- *Are we all in agreement this is a 'good thing' for Islamic finance, - or - would a decentralized financial system pose an even greater challenge for Islamic finance than if it were to remain within the current fractional reserve model,*

² The sequence and order numbering of these questions are placed intentionally as per Table 2.

given for example, it may be more vulnerable to market volatility, liquidity risk, and cyber-attacks, etc. under a decentralized model?

15. Blockchain and Crypto Assets: a distributed ledger system and/or value exchange system:

- Given the recent global challenges with cypto assets (e.g., Bitcoin, Binance, volatility, etc) and even blockchain, how can they be incorporated into Islamic finance - what Sharī'ah, legal, regulatory, technical, economic, and financial issues?*
- In other words, what specific Sharī'ah concerns or objectives do these really solve, if any?*
- Are shifting toward these methods better than moving back to the original gold standard, as previously used in Islamic history & many still advocate for?*

16. Smart contracts and DApps: a programmable decentralized Islamic financial system:

- What is the potential for social communities, decentralized autonomous organizations, Defi products and services in Islamic Finance?*
- Same as above, are these new techs even warranted? Desirable? What are the Sharī'ah, legal, regulatory, technical, economic, and financial issues?*

10. Digital transformation, modern technologies such as artificial intelligence (AI) and machine learning; the Internet of Things (IoT); virtual and augmented reality (VR/AR) are even impacting Islamic financial institutions:

- How can current IFIs take advantage of these new technologies and the increasingly tech-savvy behavior of the younger generation to further their Environmental, Social, and Governance (ESG) objectives?*
- What are the Sharī'ah specific concerns these attempt to address or resolve, if any? Are these merely addressing 'maqasid' issues or other?*
- Even with their use, will anything actually change from a Sharī'ah legal or structuring point of view? Do these new technologies change or radically challenge any of the fundamental Sharī'ah concepts and structures currently practiced in Islamic finance?*
- Is there uniformity among scholars as to their Sharī'ah uses and limits?*
- Though these products are still evolving, can we start to place measures or universal rules to protect or guide from their misuse or abuse, or is this too early?*

- *At the start of the workshop, we highlighted the growing challenges of the current monetary system – e.g., increased bank failures, inflation, volatility, etc. – Will any of these challenges be resolved by the use of these fintechologies by Islamic finance?*

12:50 p.m. Summary - Moderator to provide a summary of all the main points of view.

1:00 p.m. – 1:45 p.m.

Lunch

Part 3: *Green Islamic Finance 1: Goals and Ambitions*

1:45 p.m. Participants' Views - Open floor Discussion

Examining the following techniques, opportunity for each participant to explain briefly their views on their applicability, success and short-comings in meeting the social finance goals. Do you agree/disagree with the following questions and statements? ³

6. With the rise of Islamic Green finance and Green Sukuk, along with the use of the International Capital Market Association's (ICMA) Green Bond Principles (GBP) (World Bank 2020 and the ASEAN Capital Market Forum's ASEAN Green Bonds Standards, Malaysia's Sustainable and Responsible Investment (SRI) Sukuk Framework and Indonesia's Green Bond and Green Sukuk Framework, and the GCC's emphasis on reaching sustainable and carbon neutral goals, can all these be the driving force for sustained path for Islamic finance goals?

- *Since we can all universally agree that anything 'green' - related and linked to a sukuk that helps the environment must be a 'good' thing – and therefore a tayyib attribute to promote under Sharī'ah - is there anything else specifically unique from a Sharī'ah point of view about Green Sukuk or their use? Are there any unresolved Sharī'ah legal points still to be dealt with?*
- *Other than by aligning with the above-named principles, do the Sharī'ah give guidance as to how to define 'Green' for purposes of adhering to minimum thresholds?*
- *Why has Islamic finance industry not taken a more proactive role in meeting such objectives during the Sharī'ah certification process?*
- *What should be the 'measuring stick' used to ensure Maqāṣid al-Sharī'ah compliance?*

³ The sequence and order numbering of these questions are placed intentionally as per Table 2.

9. What are the key challenges and issues that still need to be addressed to propel Shari'ah Compliant Green Finance / Green Sukuk into the mainstream forms of global Islamic finance?

- *Green finance in perception and practice.*
- *Taxonomy and additionality*
- *Greenium*

3:05 p.m. Summary - Moderator to provide a summary of all the main points of view.

Part 4: Green Islamic Finance 2: Tools and Techniques?

3:15 p.m. Open Floor Discussion

Can the Islamic finance industry and Shari'ah compliant structures adopt/enhance/build-upon the initiatives of conventional green financing techniques? Are any other types not mentioned? Would there be an appetite for such?

7. What is still needed to develop Green finance / Green sukuk instruments and markets [as a mainstream product]?⁴

- *Are these challenges principally legal, regulatory, fiqh, economic, tax or other from a Shari'ah compliance perspective?*

11. Should main stakeholders formulate international Shari'ah standards on ESG disclosures and CSR reporting to unify the industry commitments towards the principle of "steward" in Islam?

- *Going back to the debates about avoiding standardization and creating unifying standards, would this not be a good cause for doing so?*

10. Through digital transformation, modern technologies such as artificial intelligence (AI) and machine learning; the Internet of Things (IoT); virtual and augmented reality (VR/AR) are even impacting Islamic financial institutions:

- *Can IFIs take advantage of these new technologies and the increasingly tech-savvy behavior of the younger generation to further their Environmental, Social, and Governance (ESG) objectives?*

8. Can they (Green finance/Green Sukuk) benefit from the tailwinds of DeFi, decentralization, cryptos, and geo instability of the conventional financial incumbent?

- *Is this purely an investor appetite discussion, rather than of Shari'ah structuring? Are these events irrelevant to their use, do you agree?*

⁴ The sequence and order numbering of these questions are placed intentionally as per Table 2.

- *Traditional concepts of waqf, zakat, sadaqat, qard alhassan and even takaful have all been associated with various forms of charitable or socially beneficially financings – Can and/or should these be linked to Green finance/Green sukuk? Is there investor appetite for such?*
- *How can sukuk investors be incentivized to invest ethically if they are far more concerned about the underlying investment returns?*
- *Other than Green sukuk, do any of the following have real promise?:*
 - Social impact waqf crowdfunding
 - Cash waqfs
 - SRI sukuk / Sukuk Ihsan

Other forms of green and social financing techniques (Gassner, 2020):

- 1. Frontloading
- 2. Guarantees, Partial Risk Guarantees, & First Loss
- 3. Debt-swaps/Buy-downs
- 4. Insurance Schemes
- 5. Contingency Fund
- 6. Line of Contingency Credit
- 7. Catastrophe Bonds
- 8. Humanitarian Collateralized Blended Bond
- 9. Solidarity Taxes⁵

Part 5:	CBDCs: Solution or Cause of Problems in the Cryptoworld? and Concluding Remarks
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4:00 p.m. Summary and Open Floor Discussion

Participants to discuss—and, where possible, reach a consensus on—points or issues within areas to be raised by the Moderator.

13. The Central Bank's Digital Currency (CBDC): *How Does it Impact on Cryptocurrencies?*

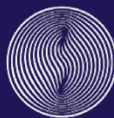
14. Can CBDC be an alternative option to cryptocurrencies and crypto assets? Or does this have no useful or meaningful impact for Islamic finance?

- *'Tools for Slavery' vs 'Tools for Freedom'*

4:30 p.m. Discussion on Future Workshop and Action Plan – Participants to assist the Moderator in drafting the workshop summary including suggested solutions.

5:00 p.m.	End of Workshop
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⁵ Gassner, Michael. Stakeholder Approach as key for Islamic Product Innovation, World Congress of Muslim Philanthropists / Global Donors Forum. SOAS Islamic Finance Workshop 2020 Pre-Workshop Notes. February 2020.



مركز قطر للمال
Qatar Financial Centre

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