

Best Practices in using Zakah to support Microenterprises Programs

أفضل الممارسات في استخدام الزكاة لدعم البرامج المتناهية الصغر

Mikro Programları Desteklemek İçin Zekat Kullanımında En İyi Uygulamalar

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INTRODUCTION

Zakah is one of the most effective tools in the Islamic fiscal policy and economic system that has been introduced to achieve a variety of socio-economic objectives. On top of those objectives are poverty alleviation and wealth redistribution. The former objective is clearly indicated in the hadith that is narrated by imam al-Bukhari when the Prophet (PBUH) commanded Mu'adh bin Jabal, his delegate to govern Yemen: “Inform them (the people of Yemen) that Allah has made a charity obligatory upon them, that is collected from their rich and given back to their poor.

In contrast, currently, estimations of zakah amounts that are estimated to be payable by Muslim individuals around the world ranges from US\$ 76 billion UNHCR (2019) to as much as US\$600 billion (UNICEF, 2019). Other estimations are also found in the literature including the estimation of Shaikh al-Qaradaghi, Zakah might reaches about 400 billion (Al-Taher, 2017) billion. In addition, the Islamic Development Bank that estimated zakah to reach \$230 - \$560 billion.



Such huge potential of zakah funds, can substantially contribute to closing the widening financial deficit in humanitarian efforts. According to the latest UNHCR reports, a funding gap of over \$4.5 billion for 2020. This represents approximately 51% of total funds needed. (UNHCR, 2020). According to the report, in the first six months of 2020 the fund managed to collect \$55.2 million in Zakat and Sadaqah funds. The funds are expected to help over 1.8 million IDPs and refugees by the end of 2020. (UNHCR, 2020a). Since its onset in 2016 to 2019 the fund has managed to raise and distribute around \$14.4 million to approximately 6,888 families located in Lebanon, Jordan, and Yemen, (UNHCR, 2019).

To accomplish the above-mentioned SDGs, an integrated microenterprise-zakah support programs could potentially hit two birds with one stone; on one hand it will achieve the SDG on poverty alleviation and on the other hand it will secure the financial sources needed to achieve that purpose. Empowering the poor is recommended in Islam.

This paper explores the viability of using zakah funds as a source of funding in Micro Enterprise Support Programs (MSP) for (SMEs). The paper highlights two case studies where zakah funds are used in financing microenterprises, the first case study is in Malaysia and the second one is in Indonesia.

Research Objectives

This paper attempts to achieve the following objectives:

- a) To survey the latest literature on zakah in the context of microenterprise support programs,
- b) To shed light on the implementation of zakah in financing microenterprise in Malaysia and Indonesia

Research Questions

Based on the research objective, this paper is going to answer the following questions:

1. What the latest literature on using zakah funds in the context of microenterprise support programs?
2. How zakah funds are utilised in offering zakah fund to support microenterprise in Malaysia and Indonesia?

Definition Of Social Finance

Social finance is generally known as an impact investment or social investment, in other words, it is a financial strategy to overcome social and environmental problems and to generate both social and financial returns. Social finance is defined as “An approach to managing investments that generate financial returns while including measurable positive social and environmental impact”.

Scope Of Social Finance

From the definition we can derived the approximately scope of social finance, which we can divided into three aspects:

First: to address social and environmental issues.

Second: to generate a positive impact on society and the environment

Third: to achieve a positive social and environmental impact while at the same time generating financial returns.

Islamic Social Finance

The term Islamic social finance or Islamic finance for social good its vital component of Sustainable development, Moreover, according to UNDP to define Islamic finance its quite important to include Islamic social finance which simply defined as “Islamic Social Finance' refers to modes of finance that are rooted in Islamic ethics and intended for social benefit. These include Zakat (almsgiving), Waqf (endowments), Sadaqa (charity) as well as Qard Hasan (interest-free loans” (A Rehman, 2019).

Furthermore, it has believed that Islamic social finance should be included in the definition of Islamic finance which intern achieve three main advantages:

First, it significantly expands the sector's scale in other words by adding the potential of Zakah and Awqaf funds which is estimated by US\$1 trillion for the former and US\$2.5 for latter.

Second, social finance is far more inclusive and widely adopted.

Third, social finance embodies key values, such as generosity and concern for others (A Rehman, 2019).

Microfinance and Microenterprise Programs

Microcredit programs have proven to be an effective measure in freeing people from poverty toward more economic inclusive in the society, Micro-enterprise development programs are strongly impacting poverty reduction, enhance employment rate, and develop the community and nation is well recognized (Terano et al., 2015).

The Malaysia's report on Millennium Development Goals indicated that employing microcredit scheme has major impact in increasing the income of the poor people in Malaysia particularly among the women. To be more specific, the extreme poverty rate in Malaysia had noticeably dipped from 16.5% in 1990 to 0.6% in 2014.


According to Che Supian, and Norziani (2012), Kedah state in Malaysia has shown that the average income of the borrowers increased from RM1,286.77 before joining microcredit to RM2703.63 after joining the programs which represents an increment rate of about 110% or RM1,416.86 to their income before joining the program. The group of "extreme poverty" fell from 12.8% (before) to 2.3% (after). The group of "poor" dropped from 19.8% (before) to 5.2% (after), and those who were in the category of "low income" fell from 54.1% (before) to 44.8% (after). The later figures and statistics indicated that microcredit has a positive effect on increasing the income of the borrowers, thus reducing the poverty rate.

Zakah-based Microenterprise Support Programs: Two Selected Case Studies

Case One: Malaysia- Selangor Zakah Board (Lembaga Zakat Selangor- LZS)

In Malaysia, the administration of zakah funds falls under the State Islamic Religion Councils (SIRCs). A total of 14 SIRCs over Malaysia where 13 of it is belong to the state and one for Wilayah Persekutuan KL (Razimi et al., 2016). Furthermore, zakah in Malaysia is under the mandate of the Department of Wakaf, Zakat, and Hajj (JAWHAR). JAWHAR was set up on March 27, 2004 (6 Safar 1425H) by former Prime Minister Tun Abdullah Ahmad Badawi. (JAWHAR, 2020).

Zakat collection in Malaysia has increased over the past decade. Remarkably, the amount of zakah funds vary from state to state. However, a noticeable increase in Zakah funds between 2007 and 2016. In Selangor state for instance, zakah funds reached approximately RM 673.7 million in 2016 compared to 202.2 million RM in 2007.



Currently, during the COVID-19 pandemic lockdowns which aims to prevent transmission COVID-19, Selangor Zakat Board (MAIS) has distributed RM232.2 million to 8 asnaf groups including more than 57 thousand asnaf families Poor as well as more than 6 thousand converts. While zakah collection in Selangor shows a decrease of 0.1% from RM253.1 million (2019) to RM252.7 million (2020) for the same period.

Moreover, the Selangor Zakat Board (LZS), due to the COVID-19 pandemic, has assigned MYR 15 million as an emergency relief fund to assist the small vendors and hawkers who are affected by the thirteen-day movement control order (MCO) imposed in the country.

Zakah Microfinance Program System

In relation to zakah, LZS adopts a system whereby the traditional eighth categories of zakah recipients are classified into two main categories: productive and non-productive, according to recipients' physical skills and abilities. Thus, the distribution of funds has been classified into consumption and productive purposes, the latter one is known as Zakah microfinance.

Interestingly, the zakah microfinance program contains not only capital seed but also training on business management and monitoring throughout the business course.

The following procedures have been implemented in the program:

1. Strict examination is undertaken to the applicants to ensure the eligibility criteria which include proper skills, business interest and desire to learn along with the physical capabilities.
2. Providing the knowledge and guidance to the recipients before and during the conduct of business.
3. Capital is given in the form of equipment and working capital such as machinery and rental premises.
4. Recipients will be given a basic course of business, including financial management and motivation before starting a business.
5. LZS would provide spiritual knowledge and religious practices such as trust, honesty, sincerity, and
6. Monitoring of applicants and their business. Monitoring will include not only business performance but also spiritual aspects, daily necessities, housing conditions and income.

From 2008 to 2010 the total number of recipients reached 1054 and the funds distributed reached RM 6.862.938 the details are in the table below.

Table 3. Number of recipients of capital assistance 2008-2010

Program	Number of Recipients			Total
	2008	2009	2010	2008 – 2010
Business Capital Assistance	299	234	356	889
Fishery Capital Assistance	21	8	50	79
Livestock Capital Assistance	8	12	11	31
Agricultural Capital Assistance	15	22	18	55
Total Recipient	343	276	435	1054
Total Distribution (RM)	1,806,753.	2,593,854	2,462,331	6,862,938
Average amount of distribution per recipient	5,267.50	9,398.02	5,660.53	6,511.33

Case Two: Baitul Maal Muamalat Indonesia (BMMI)


Indonesia is considered as a significant key player in poverty alleviation, since Indonesia is the biggest Muslim country which is 85 percent of total population in Indonesia or 216.66 million populations (BPS, 2015), Indonesia has several Zakat institutions such as, BAZNAS, BAZNAS Province, BAZNAS Regency/City and certified zakat institutions (LAZ). The National Board of Zakat (BAZNAS) is the coordinator which is responsible for managing zakat funds in Indonesia. In addition, BAZNAS has a responsibility to collect a regular report from Certified Zakat Institution (LAZ). Minister of Religious Affairs Decision (KMA) No. 333/2015 about guidelines for licensing Certified Zakat Institutions (LAZ) which led The National Board of Zakat (BAZNAS) has an authority to recommend The Certified Zakat Institutions to have official license (INDONESIA ZAKAT OUTLOOK, 2019).

Baitul Maal Muamalat Indonesia (BMMI)

BMMI is a licensed zakat organization in Indonesia that collects Islamic charities (zakat, sadaqa and waqf) and disburses the funds for the society purposes.

Seventy percent of its funds are distributed for economic empowerment through microfinance programs. (Yumna, 2019) BMMI in Indonesia has three major programs to include the poor within the microfinance system. One particular program for micro entrepreneurs called Komunitas Usaha Mikro Muamalat Berbasis Masjid (Micro entrepreneur community based on mosques/KUMMMM). This KUMMMM program is especially designed for micro entrepreneurs who actively participate in the local mosque. The key objectives of the program are firstly, to work toward economic empowerment of the poor and secondly to support religious education for society.

All BMMI KUMMMM microfinance program activities, are conducted in the mosques including client selection, mentoring and loan repayment arrangements. (Yumna, 2019) the main objective of conducting the activities in the mosque is centralizing these activities in the mosque, the institution believes that it will be able to choose clients who are motivated towards and committed to the adoption of positive attitudes and values. These client characteristics may go some way to reduce asymmetric information and moral hazard problems.



The data on the program is available for the year 2011 and 2012. It indicates that in 2011 the program has dispersed around \$435,811 and in 2012 it dispersed about \$236,426. as for the repayment rate and non-performing financing, the data reveals that in 2011 around 56% with a non-performing financing 43% however the rate was even worse in 2012 with a repayment rate of about 20% and non-performing financing about 80%. The low repayment rate in fact undermines the whole idea of mosque centralisation and commitment etc. however it is believed that low repayment rate is attributed to:

1. lack of human resources
2. public perceptions of zakat

In fact, this is very low repayment rate compared to other similar microfinance institution such as Amana Ikhtiar Malaysia which reported in 2012 very high repayment rate of 99.35%. (Abdul Rahman et.al. 2013) at this is one of the challenges that encounter humanitarian agencies when providing commercial services.

CONCLUDING REMARKS

- From the two programs of microenterprise support, it can be deduced that zakah funds constitute a great potential of funds that can significantly contribute to address the lack of financial resources to financing such programs.
- The best practice in microenterprise support programs actually start with the participants' selection process. Screening the targeted clients is essential for the success of MSPs. This is to ensure eligibility of participants to the program. It is already acknowledged that not all poor and needy persons are potential entrepreneurs. Additionally, best practices in MSPs means that microenterprise programs must include both financial and non-financial services.
- Non-financial services Include business management training, skill upgrading, monitoring, counselling.

- It is interesting that the LZS program in Malaysia includes also religious and spiritual training and sessions to encourage participants on Islamic ethics and values that are believed to enhance the commitments of the participants and the repayments of their liabilities.
- Another point of best practices as adopted in the LZS program is that cash is not provided to participants, but capital is offered in the form of equipment and working capital such as machinery and rental premises.
- The last point to be highlighted pertains to the concern on the very low repayment rate in the BMMI KUMMM program about 20% and non-performing financing about 80%. As discussed earlier, possible reasons could be the misperception on the program among participants. For that reason, it is strongly advised that participants in zakah-based programs and the alike must not be informed on the source of funding, this is to avoid the moral hazard that consequently happened by the participants and could possibly demotivate them to pay back their liabilities.

Turkish Ozet

Bu makale, Mikro Kurumsal Destek Programlarında (MSP) Küçük ve Orta Ölçekli İşletmelerin finansmanı için zekat fonlarının kullanmanın uygun olup olmadığını araştırmaktadır. Makale, zekat fonlarının mikro işletmelerin finansmanında kullanıldığı iki vaka çalışmasını ele almaktadır; ilk vaka çalışması Malezya ve ikincisi Endonezya'dadır.

Araştırma Amaçları

Bu makale aşağıdaki amaçlara ulaşmaya hedeflemektedir:

- Mikro işletme destek programları bağlamında zekatla ilgili güncel literatürü araştırmak ve sunmak,
- Malezya ve Endonezya'daki mikro işletmelerin finansmanında zekat uygulamasını örnekleriyle göstermek
- **Araştırma soruları**

Araştırma bu konu ile ilgili aşağıdaki soruları cevaplamayı hedeflemektedir:

- Mikro işletme destek programları bağlamında zekat fonlarının kullanımına ilişkin güncel literatür ne aşamadır?
- Malezya ve Endonezya'daki mikro işletmeleri desteklemek için zekat fonu nasıl kullanılmaktadır?

Bulgular

- Mikro işletme desteđi programında görüleceđi üzere zekat fonlarının, bu tür programları finanse etmek için mali kaynak eksikliđini gidermeye önemli ölçüde katkı sağladığı ve büyük bir fon potansiyeli oluşturduđu sonucuna varılabilir.
- Mikro işletme destek programlarındaki uygulamanın verimli bir şekilde işleyebilmesi katılımcıların başarılı bir şekilde belirlenmesi süreciyle başlar. Başvuran müşterilerin çok iyi bir şekilde incelenmesi Mikro işletme desteđi programın başarısı için esastır. Bu durum katılımcıların programa uygunluđunu sağlamak için önem arz etmektedir. Tüm yoksul ve muhtaç kişilerin potansiyel girişimci olmadığı zaten kabul edilmektedir. Ek olarak, Mikro işletme desteđi programındaki en iyi uygulamaların sadece finansal deđil finans dışı hizmetlerinde sunulmasıyla gerçekleştiđi görülmektedir. Finans dışı hizmetlere işletme yönetim eğitimleri, beceri geliştirme programları, denetleme ve danışmanlık hizmetleri örnek olarak verilebilir.
- Malezya'daki LZS programının, katılımcıların taahhütlerini ve yükümlülüklerinin yerine getirmesini pozitif yönde etkilediđine inanılan İslami etik ve deđerler konusunda katılımcıları teşviki için dini ve manevi eğitim içermesi ilginçtir.
- LZS programında benimsenen en iyi uygulamaların bir başka noktası da, katılımcılara nakit verilmemesidir. Sermaye genel olarak ekipman, makine ve kiralık tesisler gibi uygulamayla başvuranlara takdim edilmektedir.

Thank you