



SPECIAL SEMINAR  
HARVARD LAW SCHOOL - OCTOBER 13, 2010

## ISLAMIC FINANCE: CREATING AN ENABLING ENVIRONMENT: A SHORT REPORT

On October 13, 2010, the Islamic Finance Project (IFP) and Islamic Legal Studies Program (ILSP) held a seminar entitled “Islamic Finance: Creating an Enabling Environment.” The discussion was the second of a two-day series on Islamic finance’s structural context and how that affects its ability to impact economic development as well as fulfill its larger socioeconomic objectives.

Although Islamic finance was conceived as a system that includes broader socioeconomic goals outside of profit, it has largely operated within an economic and regulatory environment that has created impediments in the realization of those goals. The intent of the seminar was to thus explore the question: what can be done to create an enabling environment for Islamic finance to not only be commercially successful, but also deliver on its broader objectives?

The panel featured speakers from Fajr Capital Limited, Islamic Development Bank, and Harvard Law School, allowing a unique blend of academic and industry perspectives. The ensuing discussion was further enriched by the participation of the audience in the Question and Answer session.

The session began with an introduction by Nazim Ali, Executive Director of IFP and Acting Executive Director of ILSP, and Frank Vogel, Founding Director of ILSP, who introduced the panelists and pointed both to the success of Islamic finance in the past few decades and to new questions it is facing in the fields of justice, social welfare, and economic development.

Iqbal Khan, Founding Chief Executive Officer of Fajr Capital Limited, was the first presenter. After providing some historical background on the development of Islamic finance from its origins in consumer to business (C2B) mode to both micro and macro level operations in dozens of countries, he emphasized the need to create enablement and change from within the industry. Specifically, competent governance is crucial. He asserted that robust and effective corporate governance within Islamic Finance can be achieved by measures such as establishing independent Board Committees that focus on audit and risk management, as well as protect employees and members of the management by establishing whistleblower policies that protect them when they identify and report malpractice and unethical behavior. A Board of Directors which establishes an HR and Remunerations Committee is also needed which better distributes benefits to all employees rather than the top few and implements policies and standards which avoid the dangerous shift from owner’s capitalism to manager’s capitalism. Other challenges he identified were the lack of requisite experience or knowledge for people at the helm of the industry, the difficulty in incorporating younger generations through structured training programmes, the need to engage think tanks and other researchers, and the industry’s capacity to serve other communities.

Umer Chapra, Adviser to the Islamic Development Bank, was the following presenter. He emphasized that Islamic finance has the form and potential to achieve its goals, but is lacking in spirit. Like Khan, he stressed that effective corporate governance is key to improvement; he identified the Shariah board as the most significant role-playing party that needs to be particularly careful of avoiding any failures, and proposed a Supreme Shariah Board composed of individuals who are not on any other board and pressured by management or financial incentives to support bank policy. He also noted the need for central banks to play a greater role in improving the system, particularly through A&A standards and effective laws that provide appropriate supervision and regulation. Aside from supervision, he also emphasized the importance of ensuring that the banking system benefits everyone in society through more equitable resource distribution.

Samuel Hayes, Jacob H. Schiff Professor Emeritus of Harvard Business School, began by noting the infrastructure, institutes, and proliferation of practitioners Islamic finance can now boast, as well as its sympathetic supporters in the US and UK governments. Going forward from here, Islamic finance needs to complement conven-

tional finance and unburden itself of the unrealistic notion of being able to replace it. He then opened the floor for questions.

The audience raised a host of interesting questions for discussion. The first asked how Islamic finance can be scaled to a more macro level. Khan emphasized the need for governments to make commitments and implementation according to Islamic finance principles, noting that Malaysia is one of the only countries with a comprehensive Islamic finance system. Hayes added that the benchmark these countries create cannot be in a vacuum, but rather congruent to the conventional system. Another audience member asked what efforts are being made to uplift economically marginalized Muslims. Khan noted that some retail banks in the Middle East are engaged with the less privileged, but that much more needs to be done, particularly with small businesses. Chapra added that interest free loans are crucial for these customers, and if their businesses succeed, it is expected that the loan be returned and a donation provided. Other questions drew on the topics of social entrepreneurship and social responsibility, which the panelists responded should and are gradually being incorporated into Islamic finance.