



# DECENTRALIZED ASSETS, BANK FAILURES AND GREEN FINANCE

TIME FOR A SHARĪ'AH-COMPLIANT  
MONETARY SYSTEM?

## WORKSHOP AND PUBLIC LECTURE REPORTS

14 and 15, June 2023

Editor

**Dr Jonathan Ercanbrack**

Chair, Centre for Islamic and Middle Eastern Law

Foreword

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Professor of Laws and Deputy Head of the  
SOAS School of Law





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## THE SOAS-QFC PUBLIC LECTURE AND WORKSHOP ON ISLAMIC FINANCE

### **Decentralized Assets, Bank Failures and Green Finance:** Time for a Shariah-Compliant Monetary System?

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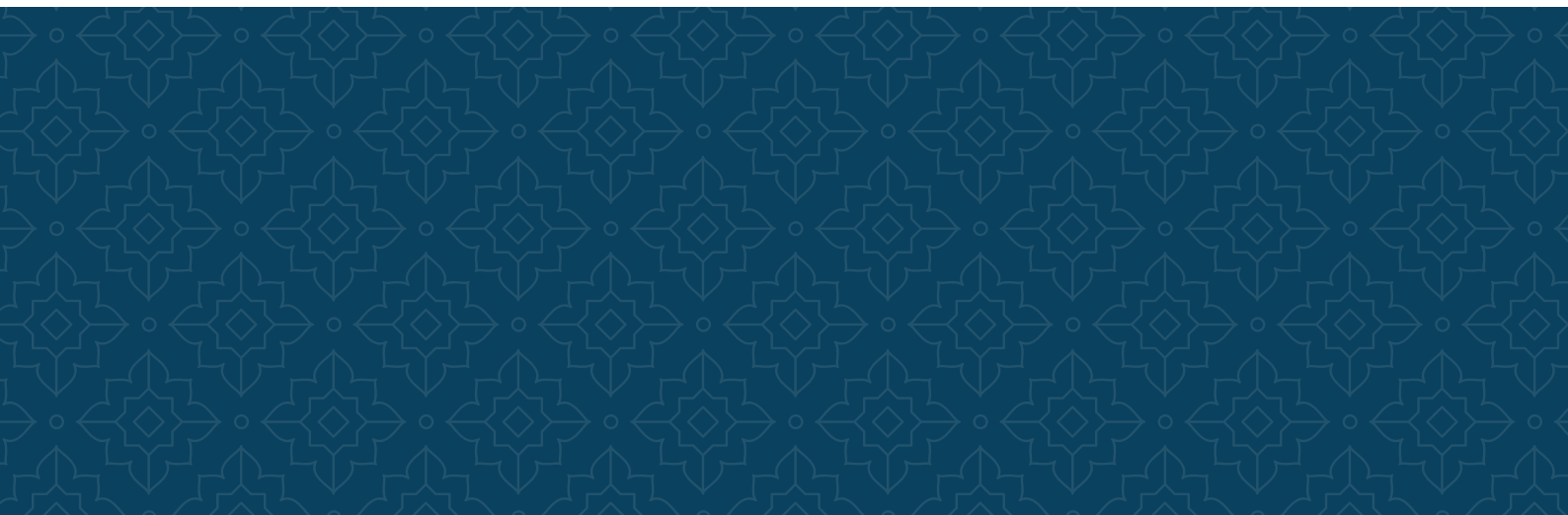
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## FOREWORD

This report provides a summary of the 2023 annual SOAS-QFC Public Lecture and Workshop on Islamic Finance held at SOAS, University of London on 14th and 15th June 2023. Contextually, the history of this event goes back to the Islamic Finance Project (IFP) initiated in 1994 by Dr Syed Nazim Ali under the Islamic Legal Studies Program at Harvard Law School, which led to the first Islamic finance workshop held at Harvard University in 2006. This was followed by an annual joint Harvard and London School of Economics (LSE) Public Lecture and Workshop on Islamic Finance held at the LSE in London from 2007 to 2014. Harvard eventually ended the IFP in 2014, but due to the perceived need to continue the engagements on Islamic finance, the event was continued under a new collaboration between Hamad Bin Khalifa University (HBKU), Doha, and LSE from 2014 to 2017. From 2018, the event has been hosted at SOAS, University of London, by the SOAS Centre of Islamic and Middle Eastern Law (CIMEL) under a new collaboration between SOAS and the Qatar Financial Centre (QFC) who has kindly provided financial support for the event since then. Also, HBKU and the International Shari'ah Research Academy for Islamic Finance (ISRA) at INCEIF University, Kuala Lumpur, Malaysia, have been joint academic partners for the annual SOAS-QFC collaboration at SOAS University of London since 2018.

The aim of the public lectures and workshops is to advance scholarship and contribute to the specialist debates on Islamic finance and to strengthen collaboration, knowledge exchange and innovation amongst economists, lawyers, shari'ah scholars and regulators in the field of Islamic finance. Considering the quality of the engagements and positive feedback received on the events over the years, it can be affirmed that this aim has been achieved. The lectures and workshops have evidently contributed to academic understanding, developments in industry practices and helped to educate society about the ethical role that Islamic finance can play in modern financial markets.

From the humble formal beginnings of modern Islamic banking in the 1960s, the Islamic finance industry has come a long way both in theory and practice and has evolved enormously over the past 60 years in response to the different changes and challenges in the conventional global financial sector. Evidently, the global interest in and the literature on Islamic banking and finance have increased steadily over time. For example, in a random Google search I run in London on 8th August 2011 for a paper I delivered on Islamic banking and finance at the 2011 National Conference of the Nigerian Bar Association (NBA) sponsored by the Central Bank of Nigeria (CBN), the phrase "Islamic Banking" returned a result of 5,230,000 hits in 0.09 seconds, and the phrase "Islamic Finance" returned a result of 7,220,000 hits in 0.11 seconds. Just for my curiosity on how online materials on the subject have increased in almost 13 years after that search, I again, while writing this Foreword, run a similar Google search on 26th May 2024 and, amazingly, the phrase "Islamic Banking" returned a result of 391,000,000 hits in 0.30 seconds, (an increase of about 7,500 per cent), while the phrase "Islamic Finance" returned a result of 148,000,000 hits in 0.32 seconds (an increase of 2,050 per cent). This gives a cursory insight into how the global interest in the subject of Islamic banking and finance has grown in recent times.



Interestingly, both the academic discourse and practical questions on Islamic finance have, over the years, gradually shifted from basic traditional shari'ah principles to probing engagements with the complex challenges emanating from new developments in contemporary global finance. Recent debates by Islamic finance experts have been mostly about what interventions the concept of Islamic finance can make to remedy the recurrent boom and bust cycles in the conventional global monetary system, the issues of bank failures, responsible investment, ethical financial ethics and governance, the complexities of fintech, green finance, cryptocurrencies, and digital finance generally. From an Islamic jurisprudential perspective, most of these new developments fall within the scope of fiqh of current issues (fiqh al-nawāzil) requiring deep intellectual and expert engagement with these complexities using the different methodologies of Islamic jurisprudence. This requires expertise in both traditional fiqh of Islamic finance and the principles of conventional finance based on contemporary realities. The themes of the public lectures and workshops have been selected in appreciation of these realities. For example, the theme of the 2022 event was "Cryptos: Distinguishing Hype & Realities in Islamic Finance", while the theme for the 2023 event, as shown by the title of this report, was "Decentralized Assets, Bank Failures and Green Finance: Time for a Shari'ah-Compliant Monetary System?". Similarly, the theme for the 2024 event is "Artificial Intelligence and Buy Now Pay Later: New Tools or New Threats to Financial Shari'ah Compliance". The events and the carefully selected themes provide a platform for the invited Islamic finance experts to deliberate and exchange ideas for the improvement of the theories and practice of Islamic banking and finance and identifying appropriate shari'ah-compliant interventions it can make to remedy the many emergent problems in the conventional global financial sector.

Most of the problems of the conventional financial sector may be attributed to the fractional reserve monetary system which is based principally on debt, interest, and speculation, often described metaphorically as the "bubble triangle", and its exposure to periodic crisis is well acknowledged by different leading financial experts. In the bubble triangle metaphor, the availability of money in the form of debt serves as the fuel, the markets in the form of interests serve as the oxygen and speculation in the markets serves as the heat to ignite the financial crisis fire that occurs periodically leading to busts and failures that jeopardise the financial sector with consequent negative impacts on the lives of the populace. Evidently, the "boom and bust" phenomenon continues to be a scary nightmare for many investors in the global interest-based capitalist financial system. Islamically, this is a concerning aspect of the conventional monetary system from religious, moral and legal perspectives, that the philosophy of Islamic finance challenges. Also, the aggressive interest-based conventional monetary system is largely at cross-purpose with the advancement of the concept of green finance aimed at promoting sustainable development priorities. While there is an agreed general perception among Islamic finance experts that the philosophy of Islamic finance can play a significant role in remedying these shortcomings of the conventional monetary system, there is a strong argument that this requires a more radical approach than mere tinkering around the edges of the conventional monetary system. It is against this background that the 2023 workshop examined the question of whether it is time for a shari'ah-compliant monetary system as a complete alternative system to replace the conventional system. However, there is also the contention that the fractional reserve system is so entrenched that its

elimination through an alternative radical monetary system such as Islamic finance would be very difficult if not impossible in the foreseeable future. This report provides a summary of the consequential discussion and engagements on these contentions.

Over the years, the events have been organised over two days, consisting of a 2-hour public lecture that is open to the public on the first day. This is followed on the second day with a closed-door whole day workshop by invitation only and restricted to established Islamic finance experts, with a commitment to stay for the entire duration of the workshop (9.00 am to 5.00 pm) to ensure comprehensive engagement with the theme of workshop. The format of the workshop is unique to ensure productivity. The workshop theme is selected through a consultative process, whereby thoughtfully curated topics are proposed by the organising team and voted on by the experts and the most preferred topic eventually selected for the workshop. Each participant is then required to send their initial written thoughts on the workshop theme in advance based on which the Workshop agenda is prepared by a team of volunteers from diverse academic and professional backgrounds. The workshop is moderated by Professor Frank E Vogel, formerly of Harvard University, allowing participants to speak freely under Chatham House Rules. At the end of the event, a report on the workshop is prepared based on the commentaries and discussions.

We at SOAS are proud and privileged to be hosting such expert scholars and practitioners from different continents to discuss the role, importance, and development of Islamic finance in the contemporary world. We appreciate the financial support of QFC and the cooperation of our academic partners, HBKU and ISRA-INCEIF. As my co-ordinating role of the event commences this year (2024), I must acknowledge the good work of my colleague Dr Jonathan Ercanbrack who has been the SOAS co-ordinator of the event for the past 5 years (2018-2023) and from whom I am taking over from 2024. Credit also goes to several esteemed colleagues for the success of this annual event at SOAS. This includes Professor Syed Nazim Ali of HBKU, for conceptualising and initiating this event from his time at Harvard and for his commitment to its continuation over the years, and Professor Frank Vogel, Mr Husam El-Khatib, Dr Umar Oseni, and Dr Shariq Nisar for their different significant contributions in making the events a success over the years.

I wish you an enjoyable reading of the report.

**Prof. Mashood A. Baderin,**  
Professor of Laws and Deputy Head of the SOAS School of Law.

# Decentralized Assets, Bank Failures and Green Finance: Time for a Sharī'ah-Compliant Monetary System?

Umar A. Oseni

## INTRODUCTION

The 2023 Annual SOAS Workshop on Islamic Finance sheds light on a combination of important topics in the global Islamic finance industry that have been beginning to receive answers from all stakeholders. In recent times, issues related to decentralized assets, bank failures, and green finance have dominated most discourses related to the global economy; hence, there is a need to leverage the unique opportunity of the workshop to obtain perspectives from bankers, academics, Sharī'ah scholars, regulators, and lawyers worldwide with a view to proffering some practical solutions to such emerging issues. Delving into the workshop's theme and significance, discussions critically examined pertinent issues facing today's businesses and economies, particularly from the perspectives of Sharī'ah and current practices in the Islamic financial services industry. To this end, a significant outcome of the discussion, characterized by openness and a distinguished approach, aimed to assess Sharī'ah's impact on the global business environment and financial practices.

Following recent high-profile bank failures, continued high inflation, increased geopolitical tensions across the world, and general financial instability, one question that comes to mind is whether Islamic finance can continue to develop and thrive strictly and sustainably within the confines of a fractional reserve model. It is also important to understand whether a sufficient case can be made to introduce a

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\* Dr. Umar A. Oseni is currently the Secretary General of the Organisation of Islamic Cooperation (OIC) Arbitration Centre. The author acknowledges the contributions of Shariq Nisar and Syed Nazim Ali to this thematic report.

*Disclaimer:* The views expressed in this report are those of the author and do not necessarily reflect the views or policies of the Organisation of Islamic Cooperation (OIC) Arbitration Centre or any previous organisation he served. This report does not constitute legal or financial advice with respect to any matter or set of facts and may not be relied upon for such purposes.

<sup>1</sup>Participants, before coming to discuss the subject, shared their thoughts in writing enabling other participants to prepare in advance about the subject matter and other related issues.

<sup>2</sup>On the impact of Sharī'ah on the global business environment and financial practices, see generally, Mercy A. Kuo, 'The Global Impact of Islamic Finance in Asia: Identity, Innovation, Institutions.' (2011) 1(1) *Journal of the International Relations and Affairs Group (JIRAG)* 46; Ibrahim Warde, *Islamic Finance in the Global Economy* (Edinburgh University Press 2010); Adam Hanieh, 'New Geographies of Financial Power: Global Islamic Finance and the Gulf.' (2020) 41(3) *Third World Quarterly* 525; Daromir Rudnykyj, 'From Wall Street to Halal Street: Malaysia and The Globalization of Islamic Finance.' (2013) 72(4) *The Journal of Asian Studies* 831; Edib Smolo and Rafe Haneef, 'Reshaping the Islamic Finance Industry: Applying the Lessons Learned from the Global Financial Crisis.' in Habib Ahmed, Mehmet Asutay and Rodney Wilson (eds), *Islamic Banking and Financial Crisis: Reputation, Stability and Risks* (Edinburgh University Press 2014) 21; Abbas Mirakhor and Mughees Shaukat, 'Islamic Finance in a Multipolar World: Traversing the Complexities of a New World.' (2013) 30(2) *Journal of Islamic Banking & Finance*; Jonathan Ercanbrack, *The Transformation of Islamic Law in Global Financial Markets* (Cambridge University Press 2015).



Shari'ah-compliant monetary system, as some scholars have suggested. Does the world need such an alternative monetary system today? How can such a system help to solve the numerous economic challenges the world is currently facing? Conversely, an alternative approach is to explore aspects of current monetary systems and identify aspects that require reform, particularly in jurisdictions where Islamic finance assets are more than 50%.



The second major subtheme discussed, which requires further perspectives from major stakeholders, is the potential for green finance. With the rise of Islamic Green Finance, including Green Sukuk, along with the use of the International Capital Market Association's (ICMA) Green Bond Principles (GBP), ASEAN Capital Market Forum's ASEAN Green Bonds Standards, Malaysia's Sustainable and Responsible Investment (SRI) Sukuk Framework, Indonesia's Green Bond and Green Sukuk Framework, and the GCC's emphasis on reaching sustainable and carbon

<sup>3</sup>See generally, Ben Jedidia Khoutem and Hichem Hamza, 'Does PLS in Islamic Banking Limit Excessive Money Creation?' (2024) 15(3) Journal of Islamic Accounting and Business Research 422; and Omar Javaid, 'Money Multiplication in Islamic Banking—A Discussion on Its Impact on Distributive Justice.' (2023) 3(1) Invest Journal of Sharia & Economic Law 41.

<sup>4</sup>Adam Abdullah, 'Towards Stabilization of the World Monetary System: A Shariah Perspective' (2017) 30(2) Journal of King Abdulaziz University: Islamic Economics 71.

<sup>5</sup>Dan Ciuriak, 'The Silicon Valley Bank Failure: Historical Perspectives and Knock-on Risks.' (2024) 43(3) Banking & Financial Services Policy Report 1.

neutral goals, can all be the driving forces for a sustained path for achieving Islamic finance goals. In discussing the potential of what may be regarded as Islamic Green Finance, it is pertinent to consider what is required for mainstream green sukuk instruments in global markets. Furthermore, while looking inwards, one would wonder what are the key challenges and issues that still need to be addressed to propel Sharī'ah-compliant Green Finance into the mainstream form of global Islamic finance. Can Green Finance and/or green Sukuk benefit from the tailwinds of Decentralized Finance (DeFi), cryptocurrencies, and geopolitical instability of the conventional financial incumbent?

It appears that the fintech dimension of monetary policy reforms could provide some insights into the above multipronged thematic discussion. It is therefore important for stakeholders to consider whether, through digital transformation, modern technologies such as Artificial Intelligence (AI) and machine learning, the Internet of Things (IoT), and Virtual and Augmented Reality (VR/AR) even impact Islamic financial institutions. Can Islamic financial institutions 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? From a preliminary analysis, it appears that DeFi provides a veritable opportunity for Islamic finance if properly utilized and developed. In addition, stakeholders must consider the relevance of Central Bank Digital Currencies (CDBC's) and their potential impact in reducing the dominant effect of

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<sup>6</sup> Emina Causevic, 'The Relationship Between the Performance of Islamic and Conventional Banks' in Mirsad Hadžikadić and Samir Avdaković (eds), *Advanced Technologies, Systems, and Applications II: Proceedings of the International Symposium on Innovative and Interdisciplinary Applications of Advanced Technologies (IAT)* (Springer International Publishing 2018) 256.

<sup>7</sup> Burhanudin Harahap, Inas Nurfadia Putri and Tastaftiyan Risfandy, 'Islamic law, Islamic finance, and Sustainable Development Goals: A Systematic Literature Review.' (2023) 15(8) *Sustainability* 6626.

<sup>8</sup> Early Ridho Kismawadi, Masitah Masitah, Mohammad Irfan and Razali Haron, 'Bridging Finance and Sustainability: Islamic Financial Institutions' Contributions to the Transition to Sustainable Energy.' in Khaleel Hussainey, Mohammad Irfan, Syed Ahmad Chan Bukhari and Yunyoung Nam (eds), *Issues of Sustainability in AI and New-Age Thematic Investing* (IGI Global 2024) 138.

<sup>9</sup> Muhammad Z. Mumtaz and Zachary A. Smith, 'Empirical Examination of the Role of Fintech in Monetary Policy.' (2020) 25(5) *Pacific Economic Review* 620; Muhammad Z. Mumtaz, Muhammad Zubair, Zachary A. Smith, and Zafar Mahmood, 'Do Fintech Activities Affect Monetary Policy?' in David G. Fernandez and John Beirne (eds), *Macroeconomic Stabilization in the Digital Age* (Asian Development Bank Institute 2020) 173; Christine Lagarde, 'Central Banking and Fintech – A Brave New World?' (Bank of England conference, London, 29 September 2017) <<https://www.imf.org/en/News/Articles/2017/09/28/sp092917-central-banking-and-fintech-a-brave-new-world>>> accessed 15 May 2024; and Xi Wang and Yanfei Tang, 'Does Non-bank Fintech Development Hurt the Effect of Targeted Monetary Policy Tools? Micro Evidence from China.' (2024) <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4596122](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4596122)> accessed 15 May 2024.

<sup>10</sup> Adel M. Sarea, Ahmed H. Elsayed and Saeed A. Bin-Nashwan (eds), *Artificial Intelligence and Islamic Finance* (Routledge 2021); and Mohammad Atif, M. Kabir Hassan, Mustafa Raza Rabbani, and Shahnawaz Khan (eds), 'Islamic FinTech: The Digital Transformation Bringing Sustainability to Islamic Finance.' in *COVID-19 and Islamic Social Finance* (Routledge 2021) 91;

unregulated cryptocurrencies. Beyond cryptocurrencies, it is important for stakeholders to consider the relevance of blockchain technology and smart contracts in revolutionizing modern financial systems. With the added value of Sharī'ah principles and the ethical foundations of the original value proposition of Islamic financial intermediation coupled with sustainable principles, blockchain and other modern technologies could help transform the modern monetary system.

This workshop report summarizes the major discussions and highlights the conclusions of the central themes. The conclusion of this report does not intend to provide prescriptive policy recommendations, but serves as a summary of the discussions that ensued during the workshop and provides general guidance for major stakeholders, particularly monetary authorities, with a view to introducing reforms that would have a long-lasting impact on the global financial system.

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<sup>11</sup> See Abdu Rahman RAH, Nur Indri Andriyani Yusuf and Syahrudin Kadir, 'Getting to Know Non-Fungible Tokens (NFT) and Decentralized Finance (DeFi) In The Era of Society 5.0.' (2023) 1(2) *International Journal of Islamic Finance* 149. For further analysis on decentralized finance, see Dirk A. Zetzsche, Douglas W. Arner, and Ross P. Buckley, 'Decentralized Finance (DeFi).' (2020) 6 *Journal of Financial Regulation* 172; Johannes Rude Jensen, Omri Ross and Victor von Wachter, 'An Introduction to Decentralized Finance (DeFi).' (2021) 26 *Complex Systems Informatics and Modelling Quarterly* 46; Patrick Schueffel, 'DeFi: Decentralized Finance - An Introduction and Overview.' (2021) 9(3) *Journal of Innovation Management I-XI*; Peterson K Ozili, 'Decentralized Finance Research and Developments Around The World.' (2022) 6(2) *Journal of Banking and Financial Technology* 117; Rasim Ozcan, 'Decentralized Finance.' in Tamer Aksoy and Umit Hacıoglu (eds), *Financial Ecosystem and Strategy in the Digital Era: Global Approaches and New Opportunities* (Springer International Publishing 2021).

<sup>12</sup> See a comprehensive report on CBDCs and the role of regulatory and supervisory authorities: COMCEC, 'Improving Cooperation among Central Banks in Terms of Digital Currencies: Challenges and Prospects for OIC Member Countries' (COMCEC Coordination Officer 2023).

<sup>13</sup> Blockchain technology or the Distributed Ledger Technology (DLT) has a lot of potentials beyond just the cryptocurrency. For further analysis, see Michael Crosby, Pradan Pattanayak, Sanjeev Verma, and Vignesh Kalyanaraman, 'Blockchain Technology: Beyond Bitcoin.' (2016) 2 *Applied Innovation Review* 6; Hongning Dai, Huaimin Wang, Shaoan Xie, Xiangping Chen, and Zibin Zheng, 'An Overview of Blockchain Technology: Architecture, Consensus, and Future Trends.' (IEEE 6<sup>th</sup> International Congress on Big Data 2017) 557; Arman Sargolzaei, Ben Amaba, Jeff Daniels, Saman Sargolzaei and Tareq Ahram, 'Blockchain Technology Innovations.' (IEEE Technology & Engineering Management Conference, TEMSCON, 2017) 137; Huaqun Guo and Xingjie Yu, 'A Survey on Blockchain Technology and Its Security.' (2022) 3(2) *Blockchain: Research and Applications* 1; Hong-Ning Dai, Huaimin Wang, Shaoan Xie, Xiangping Chen, and Zibin Zheng, 'Blockchain Challenges and Opportunities: A Survey.' (2018) 14(4) *International Journal of Web and Grid Services* 352; and Danny Yang, Philip Treleaven and Richard Gendal Brown, 'Blockchain Technology in Finance.' (2017) 50(9) *Computer* 14.

<sup>14</sup> Abdul Azeez Maruf Olayemi, Abdul Haseeb Ansari, Hunud Abia Kadouf and Umar A. Oseni, 'The Value Proposition of Islamic Financial Intermediation: Some Current Legal and Regulatory Challenges.' (2012) 6(11) *Australian Journal of Basic and Applied Sciences* 239.





## IS IT TIME FOR A SHARĪAH-COMPLIANT MONETARY SYSTEM?

As far back as 1985, Chapra identified the dysfunctional nature of the global economic system: "The instability has persisted and uncertainty has continued. After going through the throes of painfully high levels of inflation, the world economy has experienced a deep recession and unprecedented rates of unemployment, complicated further by high levels of real interest rates and unhealthy exchange rate fluctuations." Although these economic challenges that were identified nearly 40 years ago have always been there, they are even more prominent today. Recent bank failures have reignited the controversy regarding the need for an alternative monetary system. The question on the lips of some stakeholders is whether Sharī'ah-compliant principles, practices, and solutions could prevent such failures. Is the debt-based monetary system completely different

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<sup>15</sup> M Umer Chapra, *Towards a Just Monetary System* (The Islamic Foundation 1985) 19.

<sup>16</sup> For suggestions on the need for an alternative monetary system, see Maher Kababji, 'Why [the] Monetary System Failed and How to Restructure It.' (2015) 3(1) *The Journal of Economics, Marketing and Management* 23; Jason Hsu and Lindy Tsai, 'An Alternative Monetary System Reimagined: The Case for Central Bank Digital Currency.' (2020) 51 *Cal. W. Int'l LJ* 327; Rachael Tibbett, 'Alternative Currencies: A Challenge to Globalisation?.' (1997) 21 *New Political Economy* 127; Rosario Patalano, 'International Clearing System as Alternative Monetary Order.' (2023) 30(2) *The European Journal of the History of Economic Thought* 299; A. L. Abdrakhmanov, and L. V. Abdrakhmanova, 'Crypto Currency as an Alternative Monetary System.' (2017) 3 *Bulletin of Economics, Law and Sociology* 7; and Edward C. Prescott and Ryan Wessel, 'Monetary Policy with 100 Percent Reserve Banking: An Exploration.' (No. w22431, National Bureau of Economic Research 2016).

<sup>17</sup> Ahmet Suayb Gundogdu, 'Exploring Novel Islamic Monetary System: Islamic Way of Money Creation from Supply Chain to International Trade.' (2020) 11(2) *Journal of Islamic Accounting and Business Research* 440 and Abdulsamet



from the Islamic financial system? Following recent high-profile bank failures, continued high inflation, increased geopolitics, and general financial instability, can Islamic finance continue to develop and thrive strictly within the confines of the fractional reserve model? Is there a sufficient case to argue for a Shari'ah compliant monetary system to govern Islamic assets? Is such a system really required? To answer these questions, it is pertinent to begin with the definitions of monetary policy and monetary system.

A monetary policy is a well-thought-out policy that consists "of deliberate changes in the money supply to influence interest rates and, thus, the total level of spending in the economy. The goal is to achieve and maintain price stability, full employment, and economic growth." According to the Annual Economic Report 2022 of the Bank for International Settlement, the monetary system "is the set of institutions and arrangements that support monetary exchange. It comprises money and payment systems." According to the conventional understanding, a robust monetary system must possess the following features: safety and stability, accountability, efficiency, financial inclusion, user control of financial data, integrity, adaptability, and openness. Table 1 provides the high-level goals of the monetary system, which considers each goal under today's monetary system, the overbearing crypto universe, and the future monetary system (vision).

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Kayada and Ahmet Suayb Gundogdu, 'Fundamentals of Novel Islamic Monetary System for the Contemporary Age.' (2021) 7(2) *İslam Ekonomisi ve Finansı Dergisi* 293.

<sup>18</sup> For definitions of monetary system, see Bruno Colmant, Hubert De Vlieghe, Nicolas Legrand, 'Is the Current Monetary System Viable? What Are the Alternatives? Can Complementary Currencies Bring More Stability and Sustainability?' (Masters Thesis, Prom. Bruno Colmant, Louvain School of Management, Université Catholique de Louvain 2017) <<http://hdl.handle.net/2078.1/thesis:11303>> accessed 16 May 2024.

<sup>19</sup> C.R. McConnell, S.L. Brue, & S.M. Flynn, *Economics: Principles, Problems, and Policies* (McGraw-Hill Irwin 2009).

<sup>20</sup> Bank for International Settlement, "Annual Economic Report" (Bank for International Settlement 2022) 76.

<sup>21</sup> Ibid.

<sup>22</sup> Ibid 77.



## Table 1: High-level goals of the monetary system

High-level goals	Today's monetary system	Crypto universe (to date)	Future monetary system (vision)
1. <b>Safety and stability</b> – money needs to perform fundamental functions: as a store of value, unit of account and medium of exchange	Sovereign currencies can offer price stability, and public oversight has helped achieve safe and robust payment systems	Cryptocurrencies do not perform money's fundamental functions, and stablecoins need to import their credibility	Innovations grounded in trust in the central bank feature stable sovereign currencies and safe payment systems
2. <b>Accountability</b> – public mandates and regulation should ensure that key nodes in the system are accountable and transparent to users and society	Supervision, regulation and oversight tackle risks, promote competition and protect consumers, but public mandates may need to adapt to change	Crypto and DeFi create a parallel financial system to circumvent regulation, with no accountability to the general public	Clear mandates and regulation balance risks and benefits so as to harness innovation and stimulate efficiency
3. <b>Efficiency</b> – the system should provide low-cost, fast payments and throughput	Domestic payments are often expensive and financial institutions collect rents	High congestion and rents lead to costly transactions and new speculative incentives	New payment systems can significantly reduce payment costs and rents, supporting economic activity
4. <b>Inclusion</b> – the system should ensure universal access to basic services at affordable prices	Many people lack access to transaction accounts and digital payment instruments	Crypto and DeFi have not yet served to enhance financial inclusion	New service providers and interfaces can address barriers to inclusion and better serve the unbanked
5. <b>User control over data</b> – data governance arrangements should ensure users' privacy and control over data	Users trust intermediaries to keep data safe, but they do not have sufficient control over their data	Transactions are public on the blockchain – which will not work with "real names"	New data architectures can give users privacy and control over their data
6. <b>Integrity</b> – the system should avoid illicit activity such as money laundering, financing of terrorism and fraud	Payment systems are subject to extensive regulation, but illicit activity persists in cash and account fraud	Pseudo-anonymity is prone to abuse by illicit actors, and the DeFi sector is rife with fraud and theft; identification is needed	New technologies can help to better prevent illicit activity and improve on today's systems
7. <b>Adaptability</b> – the system should anticipate future developments and users' needs and foster competition and innovation	Payment systems are adapting to demands, but are not yet at the technological frontier	Programmability, composability and tokenisation give scope for new functions	Programmability, composability and tokenisation can be offered in a CBDC or through tokenised deposits
8. <b>Openness</b> – the system should allow for seamless cross-border use	Despite progress, cross-border payments are still slow, opaque and expensive	DeFi is by nature borderless and allows global transactions, but without adequate oversight	Multi-CBDC arrangements and other reforms mean cheaper, faster and safer cross-border transactions

Green denotes that a policy goal is broadly fulfilled, yellow that there is room for improvement and red that it is not generally fulfilled.

Source: BIS.

© Bank for International Settlements

From a prima facie analysis of the foregoing high-level goals, it appears that they are not different from the Islamic economic paradigm. However, the underlying principles differ both conceptually and practically. In Islamic economic principles, monetary policy has a broader perspective as it helps to “support the preservation of the purchasing power of money, poverty eradication, a tolerable gap between the rich and the poor, and an adequate social safety net.” At its core, Shari’ah mandates a financial system based on principles, where both parties operate on an equitable basis without either trying to gain any undue advantage or profit from the contractual relationship. In addition, under the Islamic monetary policy paradigm, although a central bank can introduce fair and equitable monetary policies, the focus on stipulating and regulating the official interest rate often utilized to provide liquidity to banks does not agree with core Islamic economic principles. Accordingly, the Islamic monetary policy has three main goals: **“a) economic wellbeing with full employment and optimum rate of economic growth; b) socioeconomic justice and equitable distribution of income and wealth and c) stability in the value of money.”**

In addition, utilizing monetary policy tools as a price control mechanism through the control of inflation contradicts the general prohibition of price control in Islamic economic theory. However, there are exceptions to the price control prohibition, which allows the monetary authority to step in extreme situations when there are price manipulation, hoarding, and profiteering. Implementing price control through a ceiling on interest rates as a monetary policy transmission mechanism could be considered a proactive measure, which contradicts the core principles of the Islamic economic paradigm.

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<sup>23</sup> Abbas Mirakhor, Hossein Askari, Zamir Iqbal, *Introduction to Islamic Economics: Theory and Application* (John Wiley & Sons 2015).

<sup>24</sup> See generally Ikram Ullah, Ilias Bantekas, Jonathan Ercanbrack and Umar Oseni, *Islamic Contract Law* (Oxford University Press 2024). For a general introduction on Shari’ah, see Mashood A. Baderin, *Islamic Law: A Very Short Introduction* (Oxford University Press 2021).

<sup>25</sup> Asyraf Halim and Md. Akther Uddin, 'Islamic Monetary Policy: Is there an Alternative of Interest Rate' (2015) MPRA Research Paper No. 67697, 11< <https://mpa.ub.uni-muenchen.de/67697/p>> accessed 16 May 2024. See M. Fahim Khan and Munawar Iqbal, *A Survey of Issues and a Programme for Research in Monetary and Fiscal Economics of Islam* (International Centre for Research in Islamic Economics, King Abdulaziz University, Jeddah and Institute of Policy Studies, Islamabad, 1981).

<sup>26</sup> For the analysis of the conventional monetary policy, see Sheila C. Dow, 'The Real (Social) Experience of Monetary Policy' in G Harcourt and J Pixley (eds), *Financial Crises and the Nature of Capitalist Money: Mutual Developments from the Work of Geoffrey Ingham* (Palgrave Macmillan 2012) 191.

<sup>27</sup> Mohamad Hashim Kamali, 'Tas'ir (price control) in Islamic law.' (1994) 11(1) American Journal of Islamic Social Sciences 25; Ahmad Asad Ibrahim, Ahmad, Radwan Jamal Elatrash, and Mohammad Omar Farooq, 'Hoarding Versus Circulation of Wealth from the Perspective of Maqasid Al-Shari'ah.' (2014) 7(1) International Journal of Islamic and Middle Eastern Finance and Management 6; Muneer Ahmed, 'The Fundamental Principles of Islamic Trading in the Light of Hoarding and Artificial Shortage of Supply.' (2019) 2(1) Journal of Islamic Civilization and Culture; Khairul Mukminin, 'Profit Maximization in Islamic Banking: An Assemblage of Maqasid Shariah Conception.' (2019) 12 European Journal of Islamic Finance; Muhammad Akbar Khan, 'Consumer Protection in Islamic Law (Shariah): An Overview.' (2016) 31(45) *Al-Az vā* 77; Ahmad Azam Othman, Aiman Nariman Mohd Sulaiman and Anees Tahir, 'Legal Regime on Market Manipulation in Pakistan Stock Market: An Evaluation from Shariah Perspective.' (2023) 5 JL & Soc. Pol'y 1; and Mohammad Saeed, Syeda-Masooda Mukhtar and Zafar U. Ahmed, 'International Marketing Ethics from an Islamic Perspective: A Value-Maximization Approach.' (2001) 32 Journal of Business Ethics 127.





Meanwhile, if the global economy faces serious problems, such as debt, it is essential to determine whether the issue stems from internal or external factors. The COVID-19 pandemic and bank failures underscore the need for restructuring to align with the interests of consumers. Whether developing an alternative to the fractional reserve system or reallocating resources in people's interests, a bold step towards acknowledging the problem is the first step toward finding a solution.

When discussing the fractional reserve system, it is important to recognize its 300-year history of efficiently creating debt. Banks create approximately 90% of the money supply, making it challenging to eliminate this entrenched system. Many economists and bankers believe that a fractional reserve system is the only way to operate. An alternative methodology involves improving equity ratios, as exemplified by the banks in Belgium and Australia. Without a pool or reserve system, this system allows for complementary currencies when a state currency fails. Fiscal and monetary policies can intervene if properly executed.

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<sup>28</sup> Jörg Guido Hülsmann, 'Has Fractional-Reserve Banking Really Passed the Market Test?' (2003) 7(3) *The Independent Review* 399; Michael S. Rozeff, 'Rothbard on Fractional Reserve Banking: A Critique.' (2010) 14(4) *The Independent Review* 497; Ludwig Van den Hauwe, 'The Uneasy Case for Fractional-Reserve Free Banking.' (2006) 3(2) *Procesos de Mercado Revista Europea de Economía Política* 143; James Angel, 'On the Ethics of Fractional Reserve Banking.' (2016) 24(3) *Journal of Competitiveness Studies* 164.

<sup>29</sup> Manuel Tacanho, 'Fractional Reserve Banking Is Fraudulent and Ruinous.' (2024) *Afrindependent Institute Paper No. 01 -EN/2024* < [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4719792](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4719792)> accessed 16 May 2024; and Murray Rothbard, 'Fractional Reserve Banking.' (1995) 45 *The Freeman* 624.

As the discussion shifts from money supply to interest and taxation systems, alternatives to *ribā* may be proposed. Since *ribā* is prohibited in Islam, alternatives are sought wherever interest is involved. There have been several suggestions regarding the need to replace the interest rate mechanism in monetary policy. One notable suggestion is the possibility of replacing the interest rate with Return on Equity (ROE), which generally complies with the core Islamic economic principles.

The main instrument of exchange today is money, which differs from the coins used during the time of the Prophet and the four rightly guided caliphs. Although money was historically based on gold, silver, and copper, it is now predominantly paper money. Money was created as a medium of exchange and not for trading against value, although historically it was based on the right percentages associated with commodities. Some experts consider the idea of reverting to the dinar or metals with intrinsic values to be vague and simplistic.

The bulk of today's money is debt-based, leading to inflation caused by debt money. Fluctuations in interest rates control bank money. While a top-down approach is advocated to address systemic problems, it reinforces government power, which may not always act in the best interests of people. Trust is frequently mentioned in discussions on Islamic finance, reflecting its historical basis in social contexts where

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<sup>30</sup> Abbas Mirakhor, Khairul Hafidzi Mohd Subky and Norhanim Mat Sari, 'Replacing the Interest Rate Mechanism in Monetary Policy: Case of Malaysia' (1st International Colloquium on Islamic Banking and Islamic Finance, Tarbiat Modares University, Tehran, Iran, Volume 1, 2017) 81.

<sup>31</sup> For a comprehensive discussion on currency during the time of the Prophet (PBUH) and the four rightly-guided caliphs, see Asmak Ab Rahman and Muhammad Ishak Razak, 'Money in Islamic Civilisation: From the Prophet Muhammad (PBUH) Until the Ottoman Caliphate.' (2021)15(2) *Money*; Salmy Edawati Yaacob, 'Study of Implementation [of] Gold Dinar as Currency.' (2012) 20(7) *World Applied Sciences Journal* 1014; Muhammad Akram Khan, 'Commodity Exchange and Stock Exchange in Islamic Economy.' (1988) 5(1) *American Journal of Islam and Society* 91; Ahamed Kameel Mydin Meera, *The Islamic Gold Dinar* (Pelanduk Publications 2002); Aang Kunaifi, Fadali Rahman, and Risca Dwiaryanti, 'The Philosophy and Authentication of Welfare Equalization in the Islamic Economy.' (2021) 4(2) *Islamic Research* 54; Adam Abdullah, *The Islamic Currency* (International Council of Islamic Finance Educators 2016); Mahmood M. Sanusi, 'Gold Dinar, Paper Currency and Monetary Stability: An Islamic View.' (2001) 9 *IJUMIJ* 143; Adam Abdullah, 'The Islamic Monetary Standard: The Dinar and Dirham.' (2020) 6(1) *International Journal of Islamic Economics and Finance Studies* 1; Andrew S. Ehrenkreutz, 'Monetary Aspects of Medieval Near Eastern Economic History.' (1970) *Studies in the Economic History of the Middle East* 37; Adam Abdullah and Kamola Bayram, 'From Money to Merely a Precious Metal a Historical Journey of Gold in Muslim World and Gold's Price Correlation with Other Financial Indicators in the Contemporary Financial System.' (2023) 10(2) *Turkish Journal of Islamic Economics*; Rory Naismith, 'Islamic Coins from Early Medieval England.' (2005) 165 *The Numismatic Chronicle* (1966-) 193; and Murat Cizakca, 'The Islamic Gold Dinar—Myths and Reality.' (2011) 3(1) *ISRA International Journal of Islamic Finance* 49.

<sup>32</sup> Murat Cizakca, 'The Islamic Gold Dinar—Myths and reality.' (2011) 3(1) *ISRA International Journal of Islamic Finance* 49; Ian Oxnevad, 'The Caliphate's Gold: The Islamic State's Monetary Policy and Its Implications.' (2016) 7(2) *The Journal of The Middle East and Africa* 125.

<sup>33</sup> Darryl J. Mitry and Thomas L. Matula, 'Debt-Based Currency and Borrowing From the Future: Is It Sustainable?.' (2012) 19(1) *ASBBS Proceedings* 615; Tony Smith, 'Debt in the Global Economy.' in Daniel Krier and Mark P. Worrell (eds), *The Social Ontology of Capitalism* (Palgrave Macmillan 2017) 145; Carmen M. Reinhart, Franziska L. Ohnsorge, Kenneth S. Rogoff and M. Ayhan Kose, 'The Aftermath of Debt Surges.' (2022) 14 *Annual Review of Economics* 637; and Patrick Collins, 'Unsustainability of Debt-Based Money.' in Information Resources Management Association (ed), *Research Anthology on Macroeconomics and the Achievement of Global Stability*, (IGI Global 2023) 1715.

basis in social contexts where trust is personalized. However, with globalization, personalized exchanges have diminished, although Islamic finance still benefits from partnership business arrangements regulated by faith-based principles. However, cryptocurrencies lack institutional trust, which makes them vulnerable to regulatory crackdowns. In Islamic law, although in normal economic situations, the state does not interfere with price fixing, currency, or what constitutes the legal tender is often determined by the state to protect and preserve public interest.

Debates over equity financing versus debt financing raise questions about subsidies favoring debt. While it cannot be unequivocally stated that equity should be preferred, debt is given more weight. Islamic finance emphasizes risk sharing, and the current preference for debt is excessive. Assessing whether Islam supports debt or equity essentially becomes a non-issue. According to Hadith, Allah assists the debtor as long as they fulfil their obligations. Debt can be either beneficial or detrimental depending solely on the type of contract and transaction. With geopolitical changes, such as de-risking and offshoring, opportunities and challenges arise. People's behavior towards financing methods is evolving, but the definition of capital remains unchanged. Venture capital, which is closest to equity funding, offers an alternative to heavy capital financing requirements.

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<sup>34</sup> Syed Nazim Ali, 'Building Trust in Islamic Finance Products and Services.' (2017) 12(3) *Society and Business Review* 356; Felicia Hui Ling Chong, 'Enhancing Trust Through Digital Islamic Finance and Blockchain Technology.' (2021) 13(3) *Qualitative Research in Financial Markets* 328; Adam Ng, Abbas Mirakhor and Mansor Ibrahim, 'On Building Social Capital for Islamic Finance.' (2015) 8(1) *International Journal of Islamic and Middle Eastern Finance and Management* 2; Imam Wahyudi, 'Commitment and Trust in Achieving Financial Goals of Strategic Alliance: Case in Islamic Microfinance.' (2014) 7(4) *International Journal of Islamic and Middle Eastern Finance and Management* 421; Tasawar Nawaz, 'Blind-Trust—A Pave Stone for Islamic Financial Institutions.' (2013) 4(6) *Research Journal of Finance and Accounting* 226; Fadul Abdulkarim Al-Bashir, Leila Lefi Hajlaouib, Mohammad Nassief and Walid Mansour, 'Trust Crisis in Islamic Banking Empirical Evidence Using Structural Equations Modeling.' (2015) 21(2) *International Journal of Business*, <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4192004](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4192004)> accessed 16 May 2024; Andrea Moro and Ibrahim Fatwa Wijaya, 'Trustworthiness and Margins in Islamic Small Business Financing: Evidence from Indonesia.' (2022) 22 *Borsa Istanbul Review* S35; and Chee-Keong Choong, Marlehan bin Mohamed and Mohd Nizam Bin A. Badaruddin, 'Trust Formation Process in Islamic Banking in Malaysia.' (2011) 5(30) *African Journal of Business Management* 11,779.

<sup>35</sup> Christopher Panal Lumban Gaol, Utzinger Morales, and Vanella Lopez, 'Juridical Review Concerning the Legitimacy of Cryptocurrency in Islamic Law.' (2022) 8(2) *At-Tasyrih: Jurnal Pendidikan Dan Hukum Islam* 115; Ismi Yonifa, 'Conception of Money in Islamic Economic Dimension.' (2021) 1(2) *Talaa: Journal of Islamic Finance* 121; and Norbert Oberauer, 'Money in Classical Islam: Legal Theory and Economic Practice.' (2018) 25(4) *Islamic Law and Society* 427.

<sup>36</sup> Francisco Covas and Wouter J. Den Haan, 'The Cyclical Behavior of Debt and Equity Finance.' (2011) 101(2) *American Economic Review* 877; Francisco Covas and Wouter J. Den Haan, 'The Role of Debt and Equity Finance over the Business Cycle.' (2012) 122(565) *The Economic Journal* 1262; and Daniel Creamer, Israel Borenstein, Martin Bernstein and Sergei P. Dobrovolsky, 'Debt and Equity Financing.' in *Capital in Manufacturing and Mining: Its Formation and Financing* (Princeton University Press 1960) 156-191.

<sup>37</sup> Mike Mariathan and Ouarda Merrouche, 'The Manipulation of Basel Risk-Weights.' (2014) 23(3) *Journal of Financial Intermediation* 300; Andrea Beltratti and Giovanna Paladino, 'Banks' Risk-Weights and Cost of Equity.' (2013) Bocconi University Working Paper <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2254420](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2254420)> accessed 16 May 2024; Andrea Beltratti and Giovanna Paladino, 'Basel II and Regulatory Arbitrage. Evidence from Financial Crises.' (2016) 39 *Journal of Empirical Finance* 180; and Tianze Ma, 'Basel III and The Future of Project Finance Funding.' (2016) 6 *Mich. Bus. & Entrepreneurial L. Rev.* 109.





Islamic finance is designed to work alongside other systems, catering to any individual who chooses it based on their assessment of the merits of each system. Money serves not only as an economic medium but also as a social and political one. Ensuring Sharī'ah compliance amid wealth control complexities requires trust at the local community level. Discussions about interest and taxation systems prompt debates about alternatives to *ribā*, focusing on principles rather than specific exchange mediums. Despite the complexity, the fundamental goal is to protect the value of money owners while ensuring compliance with Sharī'ah principles.

A good example of how Islamic finance can mainstream its principles in modern monetary systems is the Alternative Liquidity Facility (ALF) introduced by the Bank of England to ensure Islamic banks, which, by their very true nature, cannot pay or receive interest, can have an alternative mechanism of placing their funds with the central bank. The ALF, as a non-interest deposit facility, is *ribā*-free. These deposits are backed by Sukuk, which are securities in the

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<sup>38</sup> The Prophet Muhammad (PBUH) said: "Whoever takes the money of the people with the intention of repaying it, Allah will repay it on his behalf; and whoever takes it in order to destroy it, then Allah will destroy him". This hadith was narrated by Al-Bukhari. Sahih Al-Bukhari.

<sup>39</sup> Harry Sapienza and Sophie Manigart, 'Venture capital and growth.' in Donald L. Sexton and Hans Landström (eds), *The Blackwell handbook of entrepreneurship* (Blackwell Publishers Ltd 2017) 240; Josh Lerner and Steven N. Kaplan, 'Venture Capital Data: Opportunities and Challenges.' in *Measuring Entrepreneurial Businesses: Current knowledge and challenges* (University of Chicago Press for National Bureau of Economic Research 2016) 413; and Bob Zider, 'How Venture Capital Works.' (1998) 76(6) Harvard Business Review 131.



form of Islamic bonds and/or Sharī'ah-compliant investment certificates. After deducting the operating costs, the returns obtained are paid to the depositors. However, it is important to highlight that ALF is not a monetary policy tool. The Central Bank, responsible for ensuring stability in an economy, including the Bank of England, works towards this goal.

The underlying principles of the ALF allow it to function not as a replacement for or undermining of monetary policy, but as a market for change towards a wider and more equitable financial system. It covers a wider range of interests and provides valuable lessons regarding the shift from conventional paradigms. ALF, valued at approximately £200 million, is scalable to accommodate fluctuating demand. Its purpose involves providing non-interest-based banks with high-quality assets as a buffer, because institutions with formal interest restrictions cannot use conventional reserve accounts. The uptake of this facility, a measure of its success, was significant during the UK economic crisis, with Islamic banks avoiding recession.

When evaluating liquidity and lending facilities worldwide, there is a call to level the playing field when there are obstructions. Applying taxonomy is helpful for understanding these models. Although central banks are not responsible for providing guidance on Sharī'ah compliance, they undertake screening methods and due diligence. Key issues, such as credibility, third-party risk, sustainable operations, and efficiency, are ensured.

## **IMPACT OF FINTECH AND DECENTRALIZED FINANCE ON ISLAMIC FINANCE**

Having analyzed issues relating to the monetary system, it is important to explore the potential of fintech and decentralized finance (DeFi) in reforming the current monetary system. This analysis requires further consideration of the compatibility of DeFi with Sharī'ah principles. The

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<sup>40</sup> Badreddine Berrahlia, 'Islamic Finance Dispute Resolutions in the English Courts: Past Experience and an Outlook for the Future.' (2024) 23(1) Journal of International Trade Law and Policy 14.

<sup>41</sup> Bank of England, 'Bank of England Alternative Liquidity Facility Limited Annual Report and Accounts: 1 March 2022 – 28 February 2023' (2023) <<https://www.bankofengland.co.uk/-/media/boe/files/alternative-liquidity-facility/alfl-annual-report-2023.pdf>> accessed 16 May 2024.

<sup>42</sup> Usman W. Chohan, 'Decentralized finance (DeFi): an Emergent Alternative Financial Architecture.' (2021) Critical Blockchain Research Initiative (CBRI) Working Papers, <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3791921](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3791921)> accessed 16 May 2024 ; Dirk A. Zetzsche , Douglas W. Arner and Ross P. Buckley, 'Decentralized finance (DeFi).' (2020) 6 Journal of Financial Regulation 172; Patrick Schueffel, 'DeFi: Decentralized Finance - An Introduction and Overview.' (2021) 9(3) Journal of Innovation Management I; Alberto Lluch Lafuente, James Hsin-yu Chiang and Massimo Bartoletti, 'Towards a Theory of Decentralized Finance.' (Financial Cryptography and Data Security, FC 2021 International Workshops: CoDecFin, DeFi, VOTING, and WTSC, Virtual Event, March 5, 2021, Revised Selected Papers 25 Springer Berlin Heidelberg 2021) 227; and Rasim Ozcan, 'Decentralized Finance' in Tamer Aksoy and Umit Hacioglu (eds), Financial Ecosystem and Strategy in the Digital Era: Global Approaches and New Opportunities (Springer International Publishing 2021) 57.

discussion revealed that fintech's trajectory cannot be assumed to be consistently upward, as its current usage ultimately lies in the state's regulation, even though most fintech initiatives are spearheaded by the private sector.

In Sharī'ah, accessibility to money is mandated for all individuals, regardless of their background. Historically, people acknowledged the value of the gold Dinar, while the Dirham and silver were considered equivalent currencies. Then, US President Richard Nixon suspended the convertibility of the US Dollar into gold not to eliminate gold entirely, but to control and limit the dollar's supply against gold to mitigate rising inflation. Therefore, one question that comes to mind is how DeFi can provide an alternative to the modern monetary system and stem the increasing inflation surge. For Fintech and DeFi, without proper safeguards, ordinary individuals are generally vulnerable and at the mercy of others. A distinction exists between risk and uncertainty. Unlike uncertainty, fintech involves risk, which can be measured and assessed. They can be categorized into two broad types: revolution and evolution. Evolutionary advancements, such as fractional investing, ownership, and smart contracts, foster trust, but misleading products can cause harm. However, revolutionary changes such as Bitcoin can fundamentally alter the system for better or worse. The central question revolves around trust and whether these innovations genuinely benefit the society. Given the prevalence of technology and cyber risks, which often stem from human behavior, low societal trust raises concerns about their adoption.

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<sup>43</sup>Saikat Gochhait and Suryasish Majumdar, 'Risks and Solutions in Islamic Decentralised Finance' (International Conference on Sustainable Islamic Business and Finance (SIBF), Sakhr, Bahrain, 2022) 159; Mohammad Kabir Hassan, Rashedul Hasan, and Sirajo Aliyu, 'Fintech and Islamic Finance: Literature Review and Research Agenda.' (2020) 3(1) International Journal of Islamic Economics and Finance (IJIEF) 75; Muhammad Auwalu Haruna, M. Kabir Hassan and Mustapha Abubakar, 'Cryptocurrency Tide and Islamic Finance Development: Any Issue?' in Bora Ozkan and Jongmoo Jay Choi (eds), *Disruptive Innovation in Business and Finance in the Digital World*, vol. 20 (Emerald Publishing Limited 2019) 189; Marwan Mohamed Abdeldayem, Ramzi Nekhili and Saeed Hameed Al Dulaimi, 'Cryptocurrency as a FinTech Instrument and Islamic Finance: The GCC perspective.' (2020) 12(5) Journal of Xi'an University of Architecture & Technology 2736; and Ahmet Faruk Aysan and Ibrahim Musa Unal, 'Fintech, Digitalization, and Blockchain in Islamic Finance: Retrospective Investigation.' (2022) 1(4) FinTech 388.

<sup>44</sup>Ahmad Asad Ibrahim, Mohammad Omar Farooq and Radwan Jamal Elatrash, 'Hoarding Versus Circulation of Wealth from the Perspective of Maqasid Al-Shari'ah.' (2014) 7(1) International Journal of Islamic and Middle Eastern Finance and Management 6; and Bedjo Santoso, Buerhan Saiti and Khaliq Ahmad, 'Money in Islamic Banking System.' in Nafis Alam and Syed Aun R. Rizvi (eds), *Islamic Economies: Stability, Markets and Endowments* (Springer International Publishing 2017) 99.

<sup>45</sup>See Sandra Kollen Ghizoni, 'Nixon Ends Convertibility of US Dollars to Gold and Announces Wage/Price Controls| Federal Reserve History.' (first published 1971, Federal Reserve History) <<https://www.federalreservehistory.org/essays/gold-convertibility-ends>> accessed May 16 2024; Allen J. Matusow, 'Richard Nixon and the Failed War Against the Trading World.' (2003) 27(5) Diplomatic History 767; Mark Duckenfield, '15 August 1971: Address by US President Nixon to the Nation outlining a New Economic Policy "The Challenge of Peace".' in Mark Duckenfield, *The Monetary History of Gold* (Routledge 2016) 481; and James Harold, 'Nixon, the Dollar, and the Emerging New Money Revolution.' (2021) 35(3) *The International Economy* 20.

<sup>46</sup>Andreas Schrimpf, Sirio Aramonte and Wenqian Huang, 'DeFi Risks and the Decentralisation Illusion.' (2021) BIS Quarterly Review 21; Linda Jeng and Nic Carter, 'DeFi Protocol Risks: The Paradox of DeFi. "Regtech, Suptech and Beyond: Innovation and Technology in Financial Services" Riskbooks—Forthcoming Q3' (2021) <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3866699](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3866699)> accessed 16 May 2024; Johannes



Today's society is driven by materialism and instant gratification, which necessitates changes in the financial sector. Evolution appears to be a more viable option than revolution, provided that the underlying products align with Islamic principles. With the increasing use of fintech, the possibility of systemic change arises, even in the United States, where it may not be readily allowed. The phrase "centralization of the global economy in a decentralized way" encapsulates this idea.

As discussions about the Central Bank Digital Currency (CBDC) grow, questions arise about the role of the Islamic finance industry. Scholars generally agree that the digitalization of currency does not alter its core, and Shari'ah rules can still apply, and the currency can be regulated. The proposed solutions include backing cryptocurrencies with assets and leveraging the blockchain technology. While cryptocurrencies are currently treated as investment opportunities, a shift in attitude may be warranted if fintech continues to advance.

In assessing the mediums of exchange, cryptocurrencies are akin to art purchases, with the hope of future value appreciation. Shari'ah compliance of such assets can be evaluated in more elaborate manner, including smart contracts, which could also facilitate zakat payable on such crypto assets.

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Rude Jensen and Omri Ross, 'Managing Risk in DeFi.' (Managing Risk in DeFi in CEUR Workshop Proceedings, Aachen, 2020) < [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3745568](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3745568)> accessed 16 May 2024.

<sup>47</sup> Abdulazeem Abozaid, 'Does Shariah Recognize Cryptocurrencies as Valid Currencies?' in Nader Naifar (ed), *Impact of Financial Technology (FinTech) on Islamic Finance and Financial Stability* (IGI Global 2020) 174; and Nafis Alam and Syed Nazim Ali, *Fintech, Digital Currency and the Future of Islamic Finance: Strategic, Regulatory and Adoption Issues in the Gulf Cooperation Council* (Springer International Publishing 2021).





Although some experts believe that people can lose money through crypto exchanges and DeFi solutions, it is important to avoid overgeneralization. It is important to note that losing money does not necessarily imply a scam. Various trading practices, such as bill exchanges and self-liquidating trades, involve risks tied to the business cycle. Despite associated risks, cryptocurrencies offer safety features such as reverification and geofencing. Money laundering predominantly occurs with the US dollar, with only a small fraction conducted using crypto. As a peer-to-peer system, crypto's increased usage does not pose a serious threat to banks unlike other currencies. As such, every DeFi solution should be considered on its own merit from the legal, Sharī'ah and economic perspectives to determine their suitability and compliance with the original value proposition of Islamic economic principles.

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<sup>48</sup> Mohd Faizal Yusof, Lisasari Ab Rasid and Ridzuan Masri, 'Implementation of Zakat Payment Platform for Cryptocurrencies.' (2021) 2(1) AZKA International Journal of Zakat & Social Finance 17; Aisha Putrina Sari, Irfan Syauqi Beik and Mohammad Soleh Nurzaman, 'Zakat Standard Framework of Halal Cryptocurrency.' In Mohd Ma'Sum Billah (ed), *Halal Cryptocurrency Management* (Palgrave Macmillan 2019) 275; and Nik Safiah Nik Abdullah and Siti Khalilah Basarud-Din, 'Can Bitcoin Be Used for Zakat Payment?' (2023) 17(2) International Journal of Economics & Management.

<sup>49</sup> See generally, Alexander Barkawi and Pierre Monnin, 'Monetary Policy and Green Finance: Exploring the Links' in Maya Forstater (ed), *Greening China's Financial System* (International Institute for Sustainable Development) 155.

<sup>50</sup> *ibid.*



## ISLAMIC GREEN FINANCE: GOALS AND AMBITIONS

The last piece of the puzzle, while exploring ways to reform the current monetary system, is the need to explore the relevance of Islamic Green Finance as a monetary tool. As highlighted in one report, “monetary policy has been largely neglected in worldwide discussions on green finance. Similarly, most central banks have not even started thinking about their role in helping society reach its environmental objectives and about the potential implications of environmental degradation for their mandates.” It is also important to consider the potential role of green financing in promoting environmental sustainability. In doing this, the discussion at the workshop assessed the alignment of green finance initiatives with Sharīʿah.

There appears to be a disconnect between monetary tools and green finance, prompting an evaluation of the feasibility and applicability of the emerging concept of green finance within financial systems. Many decisions made by public and private sector firms may not always align with commercial interests but are made to comply with rules and regulations. The essence of green finance is inherently contextual and varies significantly between regions, such as Germany in Europe and Abu Dhabi in the Emirates. Different stakes and dominant industries further complicate this landscape. Resistance towards green finance does not necessarily indicate a desire to evade accountability; rather, it often stems from the high costs of transition and a lack of incentive unless there are opportunities for monetization.



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<sup>51</sup> Wael Bakhit, 'An Empirical Study of the Reasons for Resistance to Green Innovations.' (2016) 5(1) International Journal of Finance & Banking Studies (2147-4486) 30; Akanksha Choubey and Meenakshi Sharma, 'Resistance Towards Green Banking Adoption in Delhi NCR: A Grounded Theory Approach.' (2020) 14(2/4) AIMA Journal of Management and Research 1; Hyoungkun Park and Jong Dae Kim, 'Transition Towards Green Banking: Role of Financial Regulators and Financial Institutions.' (2020) 5(1) Asian Journal of Sustainability and Social Responsibility 1.



From a risk perspective, environmental risks are often overlooked, with “risk” primarily associated with potential monetary losses. However, initiatives such as the B Corp Certification in the United States encourage companies to prioritize positive social impacts and adhere to inclusive and equitable systems, thereby enhancing transparency and accountability in business operations.

It is not impossible to leverage Islamic finance to achieve the desired outcomes ethically and morally, as Shari’ah compliance aligns with capital expectations and sustainable finance principles. However, companies retain individual discretion in allocating investments for green finance, often prioritizing long-term returns over environmental risks.

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<sup>52</sup> Glenn Morgan, Malu Villela and Sergio Bulgacov, 'B Corp Certification and Its Impact on Organizations Over Time.' (2021) 170 *Journal of Business Ethics* 343; Heidi Vander Bauwhede, Philippe Van Cauwenberge and Valerie Paelman, 'The Impact of B Corp Certification on Growth.' (2021) 13(13) *Sustainability* 7191; and Indrarini Laksmiana, Maretno Harjoto and Ya-wen Yang, 'Why Do Companies Obtain the B Corporation Certification?' (2019) 15(5) *Social Responsibility Journal* 621.

<sup>53</sup> Ashraf Khan, M. Kabir Hassan and Mehmet Saraç, *Islamic Finance and Sustainable Development* (Springer International Publishing 2021); Ahmed Wasiful Alam, M. Kabir Hassan and Mehmet Saraç, 'Circular Economy, Sustainable Development, and The Role of Islamic Finance.' in M. Kabir Hassan and Mehmet Saraç (eds), *Islamic Perspective for Sustainable Financial System* (Istanbul University Press 2020) 1; Asma Ait Allali and Simona Franzoni, 'Principles of Islamic Finance and Principles of Corporate Social Responsibility: What Convergence?' (2018) 10(3) *Sustainability* 637; Ahmed Tahiri Jouti, 'An Integrated Approach for Building Sustainable Islamic Social Finance Ecosystems.' (2019) 11(2) *ISRA International Journal of Islamic Finance* 246; and Aminudin Ma'ruf, Shamsheer Mohamad and Ziyaad Mahomed, 'Sustainable Finance and a Shari' Analysis of Environmental, Social and Governance (ESG) Criteria.' in Ashraf Khan, M. Kabir Hassan and Mehmet Saraç (eds), *Islamic Finance and Sustainable Development: A Sustainable Economic Framework for Muslim and Non-Muslim Countries* (Springer International Publishing 2021) 193.

## SUMMARY AND CONCLUSION

In evaluating contrasting perspectives from respondents and workshop participants worldwide, there was a consensus that the mainstream monetary system faces a significant issue largely attributable to debt, which also affects liquidity issues. The solution requires a top-down approach, but also requires informed industry-wide leadership capable of identifying viable solutions. In this context, the government plays a pivotal role, bearing in mind that governance structures and approaches vary significantly between countries. Recognizing the role of trust in governance is crucial as we redefine trust to prevent further policy failures and inflationary pressures.

In terms of monetary policy, central banks in Muslim majority countries, particularly those in the Organization of Islamic Cooperation (OIC) member states should consider the need for alternative monetary policy instruments to complement existing policies. Alternative policy instruments should be aimed at maintaining price stability, bridging the gap between the rich and the poor, a stable economy, and sustainable development. In introducing reforms, regulators could consider Shabbir's proposal as follows.

**(i) Replacing the classical loan contract by the 16 Islamic finance contracts, (ii) an exclusive monopoly of the issuing of money through a government-owned central bank, (iii) all issued money is to be placed in PLS investment accounts with banks; (iv) the central bank issues central investment certificates, to be held by banks and the public and traded in an open market as an interbank and monetary policy instrument, (v) debt trading, as well as the use of all risk trading contracts, is prohibited in financial markets, and (vi) debtors would be granted free rescheduling in case of temporary illiquidity, but penalized in case of delinquency.**

The increasing adoption of fintech in banking systems often overlooks the intended purpose in favor of isolated technological evaluation. A key distinction lies in determining whether the change brought about by Fintech is revolutionary, evolutionary, or something in between. From a Sharī'ah compliant perspective, the latter is more encouraged. Islamic law emphasizes meeting obligations, with both debt and equity finance carrying their own benefits and drawbacks.

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<sup>54</sup> Abu Umar Faruq Ahmad, Fatima El Morabit, and Md Akther Uddin, 'Is Interest Rate Suitable as a Monetary Policy Instrument for OIC Countries?', in Muhammad Tahir, Murniati Mukhlisin, Nashr Akbar and Toseef Azid (eds) *Monetary Policy, Islamic Finance, and Islamic Corporate Governance: An International Overview*, (Emerald Publishing Limited 2021) 113.

<sup>55</sup> Mehmet Saraç and Ömer Faruk Tekdoğan, 'The Problems with Fractional Reserve Banking and Proposing a Shariah-Compliant Full Reserve Banking Model.' in Taha Eğri and Zeyneb Hafsa Orhan (eds), *Islamic Monetary Economics* (Routledge 2020) 133.

<sup>56</sup> Malik Shabbir, 'Implications and Consequences of 100% Reserve Banking through Islamic Monetary System' (2021) 3(1) *International Journal of Empirical Finance and Management Sciences* 37.

<sup>57</sup> See generally, Syed Nazim Ali and Umar A. Oseni, 'Fintech in Islamic Finance.' in Syed Nazim Ali and Umar A. Oseni (eds), *Fintech in Islamic Finance: Theory and Practice* (Routledge 2019) 3; and Syed Nazim Ali and Umar A. Oseni (eds), *Fintech in Islamic Finance: Theory and Practice* (Routledge 2019).



While DeFi and fintech may reduce risk, they do not eliminate uncertainties. Institutional behavior changes and a growing affinity for technology can lead to advancements in banking systems and jurisprudence.

Finally, although green finance is generally relatively new compared with Islamic finance, the former is relatively more easily embraced. Private actors signing Green Certificates and minimizing their carbon footprints often do so to distinguish themselves and attract more investors. Value finance companies that share their Economic, Social, and Corporate Governance (ESG) statistics as part of public disclosures serve as catalysts for fundamental change to protect the environment and educate the masses. The Shari'ah perspective of green finance or what is often referred to as Islamic Green Finance is clear: these are investments that are not only Shari'ah-compliant but also environmentally sustainable. Therefore, the following summarizes the approach to the increasing relevance of Islamic Green Finance and the approach to be adopted by major stakeholders:

This emerging trend (Islamic Green Finance) provides greater opportunities for Islamic finance to attract a wider investor base and expand its role to support the sustainable objectives of finance. This will require continuous collaboration with all stakeholders to converge in standards and reporting as well as to spur innovation, reduce barriers and costs for issuers, and increase transparency and awareness for investors.

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<sup>58</sup> See Ikram Ullah, Ilias Bantekas, Jonathan Ercanbrack and Umar Oseni, *Islamic Contract Law* (Oxford University Press 2024); and Usamah A. Uthman, 'Debt and Equity Contracts in the Theory of Social Economy' (1994) 3(1) *Review of Islamic Economics* 1.

<sup>59</sup> Hyun-Sun Ryu and Kwang Sun Ko, 'Sustainable Development of Fintech: Focused on Uncertainty and Perceived Quality Issues.' (2020) 12(18) *Sustainability* 7669.

<sup>61</sup> Ahmet Sekreter, 'Green Finance and Islamic finance.' (2017) 4(3) *International Journal of Social Sciences & Educational Studies* 115.

<sup>61</sup> Marianella Piratti and Valentino Cattelan, 'Islamic Green Finance: A New Path to Environmental Protection and Sustainable Development.' in Valentino Cattelan (ed) *Islamic Social Finance: Entrepreneurship, Cooperation and Sharing the Economy* (Routledge 2018) 144.

<sup>62</sup> Adel M. Sarea and Amer Al-Roubaie, 'Green Investment and Sustainable Development: The Case of Islamic Finance.' (2019) 9(1) *Journal of Islamic Business and Management* 14.

<sup>63</sup> Securities Commission Malaysia and The World Bank Group, 'Islamic Green Finance: Development, Ecosystem and Prospects' (Securities Commission Malaysia 2019) 14.





# SUMMARY OF COMMENTARIES

SOAS-QFC Workshop on Islamic Finance

15 June 2023

## DECENTRALISED ASSETS, BANK FAILURES, AND GREEN FINANCE – TIME FOR A SHARIAH-COMPLIANT MONETARY SYSTEM?

Fares Djafri<sup>64</sup>

### INTRODUCTION

Amidst high-profile bank failures, rising inflation, and geopolitical tensions, questions have arisen about the viability of Islamic finance within a fractional reserve model and the potential for a Shariah-compliant monetary system. This paper discusses this topic in detail. It is based on the notes and commentaries shared by the workshop participants: Decentralized Assets, Bank Failures, and Green Finance – Time for a Shariah-Compliant Monetary System? held at SOAS, University of London, on June 15, 2023. Although full commentaries are extremely valuable and beneficial, this 'summary of commentaries' aims to address the risk of failure linked to the current (fractional reserve) banking system in the context of Islamic banks. It also discusses the extent to which decentralized assets and green finance would provide opportunities to move towards a stable and resilient monetary system that can help minimize the risks of climate change and use technologies to enhance societal welfare.

To serve this purpose, this report is a brief compilation, with selective editing of notes and commentaries shared by individuals prior to the workshop. A list of contributors is placed at the end of this report.

The report is divided into four sections. The first section examines decentralized assets. The second section discusses the risk of bank failure linked to the current banking system, and the third section discusses sustainable and green finance. The fourth section reports the potential for a Shariah-compliant monetary system and the way forward.

### DECENTRALISED ASSETS

Decentralized assets refer to any form of digital or physical assets that operate on a decentralized network or platform, typically utilizing a blockchain network. They are characterized as decentralized because no government or private entity supervises their issuance. Instead, they are managed by a network of users who collectively validate transactions and maintain network integrity.

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Blockchain serves as a distributed ledger that records all transactions and ownership details in a transparent and immutable manner. Blockchain is a decentralized digital ledger technology (DLT) that operates without the need for a central authority or third party. Blockchain is a computer protocol that tracks and records data using a distributed digital ledger system. The importance of this technology is evident in the fact that it allows many participants of the same network ( so-called nodes) to store and verify information/data on a single shared ledger so that everyone can see the same data. Unlike fiat currencies, no central public authority issues cryptocurrencies and their quantity and value are beyond the purview and control of the state. Instead, they are based on the interactions of decentralized actors and technologies, such as cryptography, which ensures their security, and blockchain, which prevents counterfeit and fraud.

One manifestation of decentralized assets is crypto assets, which can be broadly classified as exchange tokens (also termed cryptocurrencies), utility tokens (providing consumptive rights and access to specific services, products, or platforms), and security tokens (also termed ad investment tokens). From a Shariah perspective, security tokens are valid, as they are investment instruments representing the rights of ownership in some specific underlying assets or stocks. However, different views exist on the validity of cryptocurrencies. While some major national-level Shariah bodies (such as Indonesia, Egypt, Palestine, Syria, and the UAE) have prohibited cryptocurrencies, a minority of scholars permit them in principle.

Furthermore, cryptocurrencies suffer from economic flaws and a lack of regulation, and they are not legal tenders in any major economy. In addition, there are issues with cryptocurrencies that go beyond their legal validity. A key concern of cryptocurrencies is that their excessive price volatility hampers their ability to perform the functions of unit of account and store of value. Their high volatility conflicts with the *maqsad* of wealth protection. Other issues that conflict with this *maqsad* are lack of liquidity, settlement of transactions, non-reversal of transactions carried out mistakenly, safekeeping and securing private keys that give access to crypto assets, and exposure to cyber risks. Likewise, many crypto exchanges have closed down due to scams or hacks or have simply disappeared along with depositors' funds.

Central bank digital currencies (CBDCs) have been introduced in an attempt to overcome the volatility problem and to address these shortcomings by pegging their value to a unit of an underlying asset, often issued on blockchains, and backing the coins wholly or partially with state-issued tenders (such as the dollar, pound, or euro), highly liquid reserves (such as government treasuries), or commodities (such as precious metals).

It is worth mentioning that the introduction of CBDCs can have several impacts on cryptocurrencies, which depend on various factors, including the design and implementation of CBDCs, regulatory approaches, market dynamics, and technological developments. The relationship between CBDCs and cryptocurrencies is still evolving, and ongoing observation and analysis are required to fully understand the implications and potential synergies between these digital currencies. The key considerations are as follows:

- **Regulatory Landscape:** The introduction of CBDCs by central banks may lead to increased regulatory scrutiny of cryptocurrencies. Central banks and regulators

may assess the regulatory framework around cryptocurrencies, including issues related to consumer protection, financial stability, anti-money laundering (AML), and combating terrorism financing (CFT).

the regulatory framework around cryptocurrencies, including issues related to consumer protection, financial stability, anti-money laundering (AML), and combating terrorism financing (CFT).

- **Competition and Adoption:** CBDCs can potentially compete with cryptocurrencies as digital currencies issued and backed by a central authority. Depending on the design and features of CBDCs, they may offer advantages, such as stability, government endorsement, and widespread acceptance, which could impact the adoption and use of cryptocurrencies.
- **Integration and Interoperability:** Central banks may explore options for interoperability between CBDCs and existing cryptocurrencies. This could involve finding ways to facilitate exchanges and transactions between CBDCs and cryptocurrencies, enabling coexistence and interoperability within the digital financial ecosystem.
- **Innovation and Development:** The introduction of CBDCs may spur innovation in the cryptocurrency space. The exploration of digital currency technologies and infrastructure by central banks could lead to advancements in blockchain technology, security, and privacy features, benefiting both CBDCs and cryptocurrencies.
- **Market Dynamics:** The introduction of CBDCs may impact the overall market dynamics of cryptocurrencies, including their price volatility, investor sentiment, and market liquidity. The availability of a government-backed digital currency may influence market participants' risk perceptions and investment behavior.

#### **In the context of Islamic economics, CBDCs could potentially play several roles:**

- **Increase financial inclusion:** CBDCs could help increase financial inclusion by providing access to digital financial services to those who are unbanked or underbanked. This aligns with the Islamic principle of promoting social justice and equitable distribution of wealth.
- **Promote transparency:** CBDCs could also promote transparency in financial transactions, which is a key principle in Islamic finance. Blockchain technology, which is often used to facilitate CBDCs, allows for transparent and secure recording of transactions.
- **Enhance monetary policy:** CBDCs could enhance the effectiveness of monetary policy by allowing central banks to monitor and control money supply more accurately. This could help reduce inflation and maintain price stability, which are important in Islamic economics.
- **Facilitate zakat:** CBDCs could potentially make it easier to collect and distribute zakat funds. CBDCs can be used to track donations and ensure that they are distributed to appropriate recipients in a transparent and efficient manner.
- **Progressive value-added taxes to address wealth distribution:** A progressive value-added tax (VAT) is a tax system in which the tax rate increases with the consumption level. The goal of this system is to create a fairer tax system by reducing the burden on low-income individuals and increasing the burden on high-income ones.

For the Islamic financial market, decentralized assets—more specifically, the DLT—have huge potential as enablers for a Shariah-based monetary system. However, rather than focusing on DLT, it is what such technology is used for that matter most. The rise in central bank digital currencies

(CBDCs) could also have a significant impact on cryptocurrencies and the broader Islamic finance ecosystem. CBDCs, if designed in accordance with the Shariah principles, could serve as an alternative to cryptocurrencies and promote financial inclusion within the Islamic finance sphere.

There is no doubt that the proliferation of cryptocurrencies across the world has awakened regulators to their monetary policy role: to either strictly regulate such currencies, which most jurisdictions do not consider valid legal tenders, or provide similar alternatives that may be better referred to as digital fiat currency. Some potential cross-border legal issues that may arise from transactions using CBDCs include: How do we allocate responsibility for AML/CFT responsibilities? What are the potential liabilities in utilizing retail CBDC for payment in another jurisdiction? Because the CBDC system is centralized at each country level, is there a provision for legal liability for the centralized system at the cross-border level, if any? How does cross-border CBDCs agree with domestic legislation on legal tenders? What potential role does Islamic economics play in designing a more enduring and resilient framework for cross-border CBDCs?

Premised on the above, robust and comprehensive regulatory frameworks should be developed to ensure that the operation of decentralized assets is in total compliance with Shariah, minimize Shariah non-compliance risk to firms and individuals who utilize it, and minimize disputes and conflicts. In addition, regulatory frameworks must be developed to address consumer protection and market conduct issues, as well as the technological impact on the orderly functioning of financial markets. Such frameworks should promote benefits (*maslahah*) to the public. According to an IMF report, a sound regulatory framework for crypto assets and decentralized finance markets must be prioritized on the global policy agenda. This is particularly pressing for stablecoins, for which some business models are subject to the risk of sudden and severe liquidity pressures. The regulatory level playing field is a key priority.





## BANK FAILURES

Bank failures can have a significant impact on the monetary system, affecting the stability of both the financial system and the economy as a whole. Bank failure highlights the importance of effective risk management, regulatory oversight, and prudent banking practices to maintain the stability and resilience of the financial system. It is noteworthy that recent bank failures and untamed inflation have exacerbated the call for reforms in the conventional monetary system and even more radical views on the need for an alternative monetary system.

In recent times, the immediate regulatory response of the US Treasury, Federal Reserve (Fed), Federal Deposit Insurance Corporation (FDIC), and British financial authorities to address bank failures in their respective jurisdictions was salutary, but they were merely firefighting responses. From a risk perspective, the problem appears systemic rather than idiosyncratic. Although the one-year term facility introduced by the Federal Reserve, which banks can access when they need additional liquidity, is a welcome development, it remains a temporary solution.

The practice of liquidity and maturity transformation in the conventional fractional banking system and the use of debt-based instruments that shift risks on both the liability and asset sides introduce fragility and make banks prone to failure. Contrary to the maxim of 'substance over form,' Islamic

banks focus on compliance with Islamic law in a formalistic way and have adopted the organizational models and practices of conventional banks. In particular, Islamic banks have adopted the conventional profit-maximizing banking system, and most of their products are replications of their conventional counterparts. While this approach has enabled Islamic finance to develop Shariah-compliant alternatives to conventional products and services, replications of substances are likely to reproduce similar problems existing in conventional systems. Importantly, the replications adopt the practice of risk-shifting and dilute the ethics entailed in linking returns to risks. This is likely to make Islamic banks unstable and prone to failure when faced with negative shock. The ethical values of risk-bearing and risk-sharing that can potentially make the banking system more stable call for a different model than the debt-based fractional model that is currently being used.

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<sup>65</sup>International Monetary Fund, 'The Crypto Ecosystem and Financial Stability Challenges: Chapter 2 - Global Financial Stability Report, COVID-19, Crypto, and Climate: Navigating Challenging Transitions' (IMF 2021).

In contrast to Islamic finance, fractional reserve banking involves the creation of money through the lending process, where banks hold only a fraction of the deposits they receive as reserves and lend out the rest. This system relies heavily on interest-based transactions that are prohibited in Islamic finance.

Given these fundamental differences, it may be difficult for Islamic finance in the form of banking institutions to continue to develop and thrive strictly within the confines of the fractional reserve model. Instead, Islamic finance may need to explore alternative models that align closely with its principles. This may require Islamic finance to reinvent its approach outside the banking framework and its Shariah-unfriendly propositions, processes, and operating models. In other words, to realize its true potential, the Islamic finance industry must convincingly differentiate itself from conventional banking by returning to its roots to facilitate trade in the real economy on a profit-sharing basis rather than adopting the conventional fiat mindset of financialization.

## GREEN FINANCING

Green finance—also known as sustainable finance or green investing, with its different manifestations (ESG framework, SDGs, sustainable and responsible investments (SRI), green bonds/sukuk, VBI, etc.)—has emerged as a new trend and investment parameter. This refers to financial products, services, and initiatives that support environmentally friendly and sustainable projects, businesses, and practices. For instance, sustainable and responsible investments (SRI), which originate from a religious-based ethical background, have developed into investments with values premised on humanism, environmentalism, and/or socialism. Initially known as “ethical investments,” it metamorphosed in nomenclature through “socially responsible investments” and later into “sustainable and responsible investments” to accommodate environmental concerns. Similarly, ESG, sometimes referred to as responsible investment, considers environmental, social, and governance factors alongside financial factors in the investment decision-making process.

Green sukuk has also gained traction in recent years, driven by sustainable development goals and frameworks, such as the International Capital Market Association (ICMA) Green Bond Principles, Malaysia’s SRI Sukuk Framework, and Indonesia’s Green Bond and Green Sukuk Framework.

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<sup>66</sup>Rodney Wilson, 'The Growth of Islamic Banking and Product Development Among Islamic Retail Banks' in S. Jaffer (ed), *Islamic Retail Banking and Finance: Global Challenges and Opportunities* (Euromoney Books 2005) 18.

F. Habib, H. Furqani, R. Ansary and S. Sairally, 'Islamic Finance and Sustainable and Responsible Investment (SRI): An Ethical Dimension' (International Shariah Research Academy for Islamic Finance 2017).

<sup>68</sup> Refinitiv and RFI Foundation, 'Islamic Finance ESG Outlook 2023, Balancing Performance and Risk' (Refinitiv and RFI Foundation 2023).

<sup>69</sup> Ibid.

In fact, most green and sustainable sukuk comply with one of the International Capital Market Association (ICMA) principles, namely, the Green Bond Principles, Sustainability-Linked Bond Principles, and Sustainability Bond Guidelines.

It is worth noting that green finance is at the core of the original value proposition of Islamic economics. The Islamic understanding of sustainable finance is seen from the do-no-harm policy, where preference is given to gross net zero emissions as opposed to the dominant net-zero transition policies being adopted globally. This principle is encapsulated in Qur'an 7:56 thus: *"Do not corrupt the earth after it has been set right – call on Him fearing and hoping. The mercy of Allah is close to those who do good."* This is further buttressed in the hadith where the Prophet (PBUH) is reported to have said: *"No harm should be inflicted nor reciprocated. Anyone who causes harm, Allah will do harm to him, and anyone who causes hardship to people, Allah will do the same to him."* Therefore, Shariah is a comprehensive concept that encompasses a set of welfare objectives manifested in ethical and moral values. These ethical and moral values are in place to ensure human welfare. Over 1400 years, Shariah has legislated a number of rules and ethical codes that aim to implement sustainable development goals, such as the principles of environmental preservation, development of the community, eradication of poverty and hunger, and many other sustainable development goals.

It is worth mentioning that the significance of incorporating sustainability and adhering to ESG-related regulations at the level of Islamic finance institutions (IFIs) has emerged. This is clearly shown by the ways in which IFIs have been doing business, whereby reporting is becoming more comprehensive, encompassing ESG, SRI, and SDG concerns. Investors and financial institutions with purely Shariah-compliant mandates are increasingly expected to incorporate sustainable and responsible investment considerations into their decision-making processes, achieving alignment with Shariah principles, while also addressing purely financial considerations.

For Islamic financial institutions, the integration of ESG considerations into business practices is typically conducted from a risk and opportunity perspective that largely reflects the conventional approach. Financial relevance operates through similar channels for conventional and Islamic financial institutions; hence, both types of financial institutions are expected to respond in the same manner. However, because the baseline was developed from a conventional perspective— and, more importantly, based on issues that are financially related to investors—it may not provide a complete framework that fully meets the needs of investors and stakeholders interested in the Islamic finance industry, and it may also overlook the unique features of Islamic finance. In other words, financial institutions, investors, and social finance organizations with Shariah-compliant mandates, along with other stakeholders, will focus on and prioritize particular ESG issues differently than their conventional counterparts. It is also likely that

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<sup>70</sup> David Rand defines Greenwashing as "a practice where companies provide the public or investors with unsubstantiated or outright false information in order to mislead them about their environmental commitments in order to win over consumers. It can involve misleading or even false statements that make a company and its products or services appear environmentally friendly."

See David Rand, 'What Is Greenwashing? Definition, Examples, and How to Avoid It' (The Future of Commerce) accessed <<https://www.the-future-of-commerce.com/2022/10/25/greenwashing-definition-stats/>> 17 May 2024.



Islamic financial institutions in developed and emerging markets will approach and prioritize ESG issues differently. These differences in the prioritization of ESG issues may also depend on their compatibility with the ethical values propagated by Islam and *maqasid al-Shariah* which have emerged in contemporary Islamic financial discourses and practices. Therefore, investments in green finance would require broadening the notion of Shariah compliance to include Islamic ethical values. Yusuf al-Qardawi links environmental protection to fulfilling the *maqasid* of religion, life, posterity, intellect, and wealth. Thus, adopting the broader notion of Shariah compliance, which includes *maqasid al-Shariah* would require Islamic finance to consider environmental impacts and induce the industry to contribute to green finance.

In addition, existing sustainability frameworks lack standardized data collection processes and consistent data disclosure, leading to market confusion. Another challenge lies in measuring, quantifying, and measuring the impact of banking activities on environmental and social factors. This condition has been exacerbated by the lack of a standardized assessment scoring system that has provided an opportunity for greenwashing. One major concern among regulators and rating agencies is the prevalent practice of greenwashing in the financial sector and among corporations that intend to broaden their investors and customer bases. Unfortunately, the Islamic finance industry is not immune to these greenwashing practices. In a survey conducted in 2021 among 2000 consumers in the United States, it was found that over 50% agreed to make sustainable buying choices. However, 88% of the same consumers emphasized that they do not ordinarily trust brands that position themselves in the market as sustainable. Similarly, in the Islamic Sustainable Finance and Investment Survey 2022 conducted by IFN, 77% of the practitioners surveyed agreed that greenwashing remains a key issue in the Islamic ESG space. Beyond Islamic ESG space, greenwashing litigation has increased globally. This is a worrying trend in global business and the practices that have prompted them to be nipped in the bud.

Because of these challenges, the worldwide shift towards the incorporation of ESG criteria, which consider non-financial factors in decision-making, offers a significant opportunity for the Islamic industry to introduce its own version of ESG, shaped by the objectives of Shariah (*maqasid al-Shariah*). The General Council for Islamic Banks and Financial Institutions (CIBAFI) has already established a Sustainability Guide for IFIs. The CIBAFI Sustainability Guide presents an integral framework for assessing Islamic banks' compliance with sustainability principles and *maqasid al-Shariah*.

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<sup>71</sup> Ibid.

<sup>72</sup> Islamic Finance News, 'Islamic Sustainable Finance & Investment Report 2022' (Red Money 2022) 8.

<sup>73</sup> For instance, see the following cases relating to greenwashing in: *In re Danimer Scientific, Inc. Securities Litigation*, 1:21-cv-02708 (E.D.N.Y. May 14, 2021); *SEC v. Vale S.A.*, 1:22-cv-02405 (E.D.N.Y. Apr. 28, 2022); *In the Matter of BNY Mellon Investment Adviser, Inc.*, SEC Administrative Proceeding File No. 3-20867 (May 23, 2022); and *Ramirez v. Exxon Mobil Corporation et al*, 3:16-cv-03111 (N.D. Tex. Nov 7, 2016).  
*irates* (Graham & Trotman 1991) 204.

In addition, the recent efforts of financial regulators in some jurisdictions to clamp down on asset managers who entice investors with misleading claims of being ESG-compliant are welcome. In Islamic commercial jurisprudence, deceptive market practices (*ghabn*) and fraudulent misrepresentation (*tadlis*) are the bases for the invalidation of a contract. Such fraudulent misrepresentation in business practice is prohibited in Islamic law. One way to solve this challenge is to introduce the Green Taxonomy standard with an accompanying tool to detect greenwashing, as developed in the European Union. However, beyond such standards, the ethical dimension should be included with regular regulatory audits to protect undiscerning investors or consumers. Greenwashing in the financial sector should be prevented by carefully considering regulations to ensure that investors, consumers, and other stakeholders are well protected.

## THE WAY FORWARD: A SHARIAH-COMPLIANT MONETARY SYSTEM

Discussions about monetary policies and how the Shariah-compliant monetary system differs from the conventional system can be traced back decades to the early days of modern Islamic banking and finance. Although there are some similarities in objectives between the two monetary systems, particularly regarding achieving stability and sustainable economic growth, the differences lie in the Islamic prohibition of interest (*riba*) and, consequently, the instruments used for monetary policies. Islam does not allow instruments that contain interest rates or injuries. Instead, instruments of monetary policy in Islamic economics are based, in principle, on instruments devoid of interest. Similarly, the contemporary scholars interpreted *riba* as: 'usury or interest; an increase over the principle in a loan transaction or in commodity exchange that accrues to the lender/owner without giving an equivalent countervalue to the other party'. Accordingly, *riba* causes harm in business transactions and gives the rich in society an easy way of accumulating wealth, hence causing harm to other members of society. Shariah considers this profit as a prohibited earning that leads to laziness among the rentier class and a lack of productivity in a larger society.

Another important principle that differentiates Islamic monetary policy from the conventional one is the prohibition of *gharar* and speculation due to their obvious harm and direct link to economic instability and financial crises. The prohibition of speculation promotes economic stability and protects against the negative consequences of financial crises, as demonstrated by the relative stability of Islamic financial institutions during the 2007-2008 crisis. In fact, crises that have rocked various parts of the world in the past decades are considered, among others, to lie in monetary matters. Thus, speculation in the derivatives or foreign exchange markets cannot be part of any Islamic monetary system. In addition, many have explained the rationale behind the prohibition of *gharar* as an in-built risk management mechanism to promote real economic transactions such that parties will conduct due diligence and avoid contracts with excessive uncertainty and unnecessary ambiguity. This protects investors' funds from excessively risky exposures, thereby retaining their trust in the economy.

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<sup>74</sup> CIBAFI, 'Sustainability Guide for Islamic Financial Institutions: Guidelines for Islamic Banks' (CIBAFI 2022).

However, unlike the prohibition of *riba* which is absolute, some types of *gharar* may not necessarily render the contract null or void. According to many Muslim scholars, excessive *gharar* is prohibited, whereas trivial *gharar* is tolerated to a certain extent.

It is important to highlight that Islam, the revealed religion, has handled matters related to monetary system management by providing principle-based recommendations rather than specific operational instructions. This is done to ensure that it can be implemented regardless of time or location constraints. Below are some principles laid down by Shariah to manage monetary issues:

1. Riba (interest) is prohibited by Shariah:  
Allah declared war on people engaged in usury (*riba*). Consequently, changing the interest rate should not be the strategy used to manage the monetary system. This principle underpins the idea that money is not a commodity. This is a medium for exchange. Hence, making money from money (loans with interest) is prohibited. On the other hand, profit can be earned through trading or joint venture activities. In the Qur'an, Allah declares, '...but Allah has permitted trading and forbidden interest.' (Al-Qur'an, 2:275).
2. Money is preferably made of precious metals or materials such as gold and silver. It can also take the shape of a paper or digital currency backed by precious metals/materials.
3. The principle of wealth circulation: The original rule is that the economy should be based on natural and practical market forces that allow each person to behave normally in accordance with his or her aptitude, choice, and preferences, thus allowing his or her actions to be more fruitful, healthy, and beneficial. Under this premise, Shariah places a strong focus on preventing the concentration of wealth in a small number of hands. Allah mentions: "...so that this wealth should not become confined only to the rich amongst you." (Al-Qur'an, 59:7).
4. The fundamental principle of the contract law is permissibility. Under this premise, and as long as it is done in a Shariah-compliant manner, the government can influence the money supply of the economy by, for instance, selling and purchasing securities.

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<sup>75</sup> Susan E. Rayner, *The Theory of Contracts in Islamic Law: a Comparative Analysis with Particular Reference to the Modern Legislation in Kuwait, Bahrain and the United Arab Emirates* (Graham & Trotman 1991) 204.

<sup>76</sup> Mohamed Aslam Mohamed Haneef, Moutaz Abojeib and Mustafa Omar Mohammed (eds), *Islamic Economics: Principles and Analysis* (ISRA RMC 2018).

<sup>77</sup> Ahcene Lahsasna, *Maqasid Al-Shariah in Islamic Finance* (IBFIM 2013).





Furthermore, gold is of particular importance in the Islamic monetary system primarily because of its value, durability, and historical acceptance as a medium of exchange. It plays an important role in the Islamic monetary system, serving as a Shariah-compliant store of value, medium of exchange, and wealth preservation tools. It is widely assumed that a gold-backed monetary system has potential benefits. Because a currency's value is tied to a tangible asset with intrinsic value, it is generally more stable than fiat currency. This stability can help prevent excessive inflation and deflation by providing a reliable exchange medium for economic transactions. However, it is important to note that the gold-backed monetary system also has limitations and challenges. It requires sufficient gold reserves, which can limit the flexibility of monetary policy. Moreover, the transition from a fiat monetary system to a gold-based one can be complex and may require significant economic adjustments. Therefore, while a gold-backed monetary system offers potential benefits, its issuance is virtually impossible because of the following factors.

- a) One dinar was previously represented by a 4.25 gramme gold coin. Currently, it is worth about \$250 USD. Simply put, it is not feasible to use it as daily currency to pay for regular items.
- b) Having gold coins in circulation exposes them to fraud. The general population would be unable to verify whether the coin given to them was a real gold coin.
- c) Storing actual gold coins would take up a lot of room and would be costly (including security services and takaful/insurance).

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<sup>78</sup>As explained in the note, this is the form of money endorsed by the Prophet (PBUH) during his time. However, from a Shariah standpoint, there is no conclusive proof that the money must be made of gold. The non-gold-based *fulus* has also been acknowledged as a "supporting currency" for the dinar and the dirham.

A practical mechanism must be capable of addressing these three challenges. In addition, it must be able to resolve issues pertaining to the exchange of gold, which is considered a *ribawi* item from the Shariah perspective. In this regard, Bursa Malaysia has started an effort to develop the Bursa Gold Dinar (BGD) as an end-to-end Shariah-compliant gold investment product that is fully backed by physical gold and can be electronically traded on the BGD Platform. The BGD is envisaged to be a predominantly disintermediated market, as investors shall directly engage with the BGD Platform where Bursa will be able to offer live competitive prices to investors to invest and trade in gold.



## CONCLUSION

In summary, applying Shariah compliance in a formal legalistic sense is likely to result in a quasi-Islamic financial and monetary system with similar characteristics to its conventional counterparts. The transformation towards a resilient and sustainable financial and monetary system would require expanding the notion of Shariah compliance from the narrow formal adherence of legal regulation to compliance that integrates the ethical values and principles articulated in the *maqasid al-Shariah*. Without encompassing ethical values, an Islamic monetary and financial system based on formal legal compliance does not offer anything substantially different.

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<sup>79</sup> IFN Fintech, 'Bursa Gold Dinar to Launch Soon' IFN Fintech (March 9, 2023) <<https://ifnfintech.com/bursa-gold-dinar-to-launch-soon/>> accessed 17 May 2024.

Undoubtedly, digital assets and green finance have enormous potential to transform the economy. However, beyond rhetoric, is it possible to have an alternative monetary system in today's world? What are the basic principles and requirements of such alternative systems? Can such an alternative system provide necessary solutions to the current global economic problem? What are the key success factors of such an alternative system? One thing that we should realize is that fintech, DLT or its associated technology, and green finance are mere enablers to achieve the original value proposition of Islamic economics. In designing an alternative monetary system, the scope must be broadened to include all aspects of the economy, and key stakeholders must agree on the core pillars of such a Shariah-based monetary system, which comprises key principles, institutions, products, and solutions to world economic problems.

## ACKNOWLEDGEMENTS

**Danish Aga**, Director Technology, Bank of America Merrill Lynch, London, U.K.

**Habib Ahmed**, Durham University Business School, U.K.

**Samir Alamad**, Senior Lecturer in Finance and Associate Director, Coventry University, Chief Advisor Islamic Finance and Banking, IIFS Ltd. Coventry, U.K.

**Sharjil Ahmed**, Cykuba, London, UK.

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**Mufti Abdulkader Barkatulla**, Shariah Scholar, London, UK.

**Richard de Belder & Omar Shaikh**, Islamic Finance Council, UK.

**Michael Gassner**, IslamicFinance.de, Geneva, Switzerland.



**Salah Gueydi**, Managing Director Tax, Qatar Financial Centre Authority, Doha, Qatar.

**Farrukh Habib**, Co-Founder, Shariah Experts Ltd, London, U.K.

**Ashraf Bin Md Hashim**, Executive Director, ISRA – INCEIF, Kuala Lumpur, Malaysia.

**Harris Irfan**, CEO, Cordoba Capital Markets Ltd, London, U.K.

**Shariq Nisar**, Director, Rizvi Institute of Management and Research, Mumbai, India.

**Rodney Wilso**, Professor Emeritus, Durham University, Durham, UK.

**Umar A. Oseni**, Chief Executive Officer, International Islamic Liquidity Management Corporation, Kuala Lumpur, Malaysia





# 2023 SOAS-QFC Public Lecture on Islamic Finance

## Decentralized Assets, Bank Failures, and Green Finance: Advocating for a Sharia Compliant Monetary System

Richard Thomas<sup>80</sup>

### Abstract

Richard Thomas explores the necessity of a Sharia compliant monetary system in the context of increasing global financial instability, decentralized asset proliferation, and growing demand for ethical and sustainable finance practices. Drawing on personal experiences and scholarly influences, he argues for a system that incorporates Islamic financial principles to address inherent flaws in conventional banking and to provide a viable alternative through ethical and green finance lenses.

### INTRODUCTION

The journey in Islamic Banking & Finance began in 1981 at the Saudi International Bank in London, focusing on developing trade finance solutions for GCC Islamic Banks and the Islamic Development Bank. This experience laid the foundation for exploring Sharia-compliant alternatives within the modern portfolio context, emphasizing the critical need for a financial system that aligns with ethical and sustainable practices.

### INFLUENCES AND CONCEPTUAL FRAMEWORK

Influential works, such as Sam Hayes and Frank Vogel's 1998 book, "Islamic Law and Finance: Religion, Risk, and Return", have shaped understanding beyond mere ethical comparisons, positioning Islamic finance within a broader semantic framework. The impact of pivotal scholars and texts, including Dr Mahmoud El Gamal's work on the prohibition of Gharar (uncertainty) in Islamic jurisprudence, has redefined the relationship between Islamic finance and risk management.

I was inspired by Dr Mahmoud El Gamal's for example he suggested " if a contract can increase economic efficiency through some form of risk transfer, the prohibition of trading in risk should be applicable. Cases where such a prohibition is moot because the risk-trading instrument is not used, do not affect this general conclusion. In cases where trading in risk is inherent in the contract, but where the contract is important to meet economic needs (e.g. salam), the analysis is still useful in two regards:(i) we can consider whether or not there is a risk sharing mechanism which can reduce part of the inherent trading in risk, and (ii) we should consider such alternatives if secondary tools for managing the resulting risk are sought".

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By this, I thought that the internal Shariah Committee of the bank should be able to express their opinion about whether such analysis had been effectively undertaken and whether those proposing risks on either basis truly understood the products and risks thereof and the nature of the profits that should accrue.

Dr Gamals's paper was too dense to be easily modelled in this way and asked too much of all involved at the time. I look back now and think that I have some issues with his application of Prospect Theory and its current utility. However, generally, the times are different, and applied tools can be sought.

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<sup>81</sup> Mahmoud El-Gamal. "An economic explication of the prohibition of gharar in classical Islamic jurisprudence." *Islamic Economic Studies* 8 (2), 2001.

## The Need for Public Understanding of Islamic Financial Principles

Thomas argues that a deeper public understanding of Islamic financial principles, such as *Jehala* (ignorance), *Gharar* (uncertainty), and *Maysir* (gambling), is crucial for establishing a financial management system capable of withstanding the crises inherent in conventional banking. He highlights recent concerns about bank stability and public trust, drawing on data from Gallup and Moody's analytics to underscore the urgency of reform. A broad comprehension of *Jehala*, *Gharar*, both in its major and minor forms, and *Maysir/Qimar* is essential for crafting a financial management system that can support Islamic Banking and Finance alongside other faith-based, ethical, and green financial models.

My remarks are based on personal insights and not intended as directives or mandates. I use the term "Shariah Compliant" because it is widely recognized and understood, addressing what could be considered a layperson's familiarity with *Jehala*, *Gharar*, and *Maysir/Qimar*.

I contend that a broad public comprehension of *Jehala*, *Gharar*, both in its major and minor forms, and *Maysir/Qimar* is essential for crafting a financial management system that can support Islamic Banking and Finance alongside other faith-based or ethical and green financial models, without succumbing to the types of banking failures typically seen in Fractional Reserve Banks that potentially precipitate widespread financial crises.

In my opinion, an authentic and widespread understanding of the principles surrounding *Jehala*, *Gharar*, and *Maysir*, along with their associated prohibitions, is crucial for establishing a financial system and social contract capable of integrating a Shariah-compliant monetary framework.

Furthermore, considering the current state of conventional finance, there is significant merit in investigating this concept more deeply than ever. It is important to recognize that transformations are already occurring within the traditional monetary system and its metrics, which prompts the question of who drives Islamic Finance and the Halal Economy amidst these changes.

As conventional banks increasingly fail to meet their obligations under the prevailing, somewhat distorted, social contract of finance—and in some cases collapse entirely—space is emerging as a more trustworthy alternative. A major failure of conventional banks in recent times is their inability to maintain trust and public confidence. In the near future, it is difficult to envision improvements in this area. I believe that the lack of clarity and the presence of uncertainty and speculation, represented by *Jehala*, *Gharar*, and *Maysir*, are primarily responsible for the erosion of trust and confidence in the banking and financial sectors, moving beyond traditional notions of ignorance, uncertainty, and risk.

Ironically, I have come to realize that limited awareness and understanding of the specific principles of *Jehala*, *Gharar*, and *Maysir*, which are foundational to the Islamic financial model, could be central to the modest adoption of Islamic Banking and Finance in the West. These principles are also part of a broader, recently mainstreamed debate about moving "From *Halal* to *Tayib*." While potential clients of Islamic Banking and Finance might grasp the concept of *Riba* (and those who are not aided by organizations such as the *Riba* Free Foundation), their understanding of the other principles and their importance in establishing the inherent trustworthiness of Islamic banks is often lacking. Furthermore, there is a lack of widespread understanding of how these principles apply practically in daily economic life, which impedes broader acceptance and limits the potential for a Shariah-compliant monetary system. Although he did not delve deeply into the *Halal*-to-*Tayib* discussion, its relevance is implicit.

The scenario changes only when the average person, like the one on the proverbial Clapham Omnibus, can clearly see how their personal financial situation, the principles of *Jehala*, *Gharar*, and *Maysir*, and issues with conventional banking are interlinked. Only then can we establish a new "Natural Social Contract" in finance, providing fertile ground for a Shariah Compliant Monetary System.

## **SHARIA COMPLIANT ALTERNATIVES TO CONVENTIONAL BANKING**

As conventional banks increasingly fail to meet their obligations under a distorted social finance contract, space is emerging as a more trustworthy alternative. Thomas pointed out that the lack of clarity and the presence of uncertainty and speculation, as represented by *Jehala*, *Gharar*, and *Maysir*, are primarily responsible for the erosion of trust and confidence in the banking and financial sectors. This situation provides an impetus for exploring decentralized finance (DeFi) and its Decentralized Autonomous Organization (DAO) model as potential solutions that authentically reflect true costs, profits, and value.

## **DECENTRALIZED FINANCE AND REAL ASSET LINKAGES**

The discussion extends to the connection between the monetary system and real assets, a crucial aspect of the fiat money system. While debates like those surrounding the Gold Dinar and tangible assets continue, Thomas emphasizes the importance of reflecting "True" value in monetary systems to prevent *Gharar*. These considerations are seen as essential steps towards "Sustainability Transition" in finance.





## CASE FOR A SHARIA COMPLIANT MONETARY SYSTEM

This section outlines the theoretical and practical benefits of a Sharia-compliant monetary system, suggesting that such a system can better meet the needs of modern financial realities and ethical considerations than the existing systems. It examines the potential of decentralized finance (DeFi) and blockchain technologies to offer transparent and trustworthy alternatives to traditional banking.

Current discussions in Islamic Finance often focus on the link between the monetary system and real assets, a connection that is missing from the fiat money system. For instance, there is debate over whether an Islamic monetary system should be based on tangible assets, such as the Gold Dinar. While I remain undecided on this specific asset, the broader historical discussion has often centered on Rentier and Rentier Capitalism. I believe that rentier considerations should still play a significant role in discussions about how changes, including currency digitization, will affect the existing system.

My current view is that money and its supporting system must be able to reflect its "True" value. Until recently, it seemed unnecessary to account for this true value within the "store of value," which is money, largely because tools to do so were unavailable. If an Islamic Monetary System is based on an asset that does not reflect its true value, then the potential for *Gharar* could be greater than in the current system.

In my opinion, these considerations are essential steps towards a "Sustainability Transition" in finance. Therefore, is it time for a Sharia Compliant Monetary System? Without opening up the *Halal-to-Tayib* discussion, the answer to that question can never be no. A Shariah-compliant monetary system should be a universally acceptable solution to an increasingly serious problem. The risk is more that conventional markets are developing top down, "ethically based "green" sustainable finance models that are changing the conventional monetary system, and those standards are being developed unilaterally by those already at the table.

Similar to *Jehala* and *Gharar*, the argument will be "all Shariah finance fits in our standard, but not all our standard fits in Shariah finance, so we will have this standard because it is more comprehensive." Like the UK Islamic Banking provisions, Islamic finance will continue to be at the margin and "accommodated."

## **CHALLENGES AND OPPORTUNITIES**

The discussion includes an analysis of the challenges of integrating Islamic financial principles into mainstream finance, particularly in Western contexts. It also considers opportunities for innovation in green finance by leveraging Islamic finance's emphasis on asset-backed and ethical investment.

## **CONCLUSION: TOWARDS A NATURAL SOCIAL CONTRACT AND SHARIA COMPLIANT SYSTEMS**

Thomas suggested the establishment of a new "Natural Social Contract" in finance, providing fertile ground for a Sharia Compliant Monetary System. He calls for recognition of the role necessary for such systems to mark the evolving landscape of global finance, advocating for a universally acceptable solution to an increasingly serious problem. He warned that, if not addressed, Islamic finance might continue to be marginalized by conventional financial models, urging proactive engagement and innovation to ensure its integration and relevance.

The speech concluded by advocating for a natural social contract supported by a Sharia-compliant monetary system, which could lead to more sustainable and ethical financial practices globally. This calls for ongoing dialogue and collaboration between Islamic and conventional financial institutions to explore synergies and foster a more inclusive financial landscape.

## **FUTURE OUTLOOK**

In the future, Thomas hints at the role of advanced technologies such as AI in drafting and shaping discussions in finance. He expressed hope that tools such as ChatGPT might eventually recognize and advocate for the specificities of Shariah compliant finance, potentially turning the tables in favor of more ethical and financial systems worldwide.

For example, Bitcoin is the most recognized cryptocurrency. It facilitates peer-to-peer value exchange in the digital realm via a decentralized protocol, cryptography, and consensus mechanism on a periodically updated public ledger known as a blockchain. However, how well does an average person understand this definition? Would they consider cryptocurrency as "money"?

I am particularly interested in exploring how the value exchange aspect of cryptocurrency and intrinsic risk values—both in transfer and pricing, as informed by the Islamic prohibitions on *Gharar*—intersect and inform each other.

In my view, decentralized finance (DeFi) and its Decentralized Autonomous Organization (DAO) model must establish a transparent relationship that authentically reflects true costs, true profits, and true value, and accurately accounts for true risks, details of which I will expand upon later. However, this system may be the only viable option available.

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## **CIMEL (Centre of Islamic and Middle Eastern Law) SOAS, University of London**

The Centre of Islamic and Middle Eastern Law was established in 1990 at the School of Oriental and African Studies in recognition of the growing importance of law in both its Islamic and Middle Eastern dimensions. The analysis of the various systems of law at work in the Islamic and Middle Eastern world as well as an active interaction with Middle Eastern and Muslim lawmakers and scholars are crucial for the future of stability and for the rule of law in its various forms inside each jurisdiction. The rule of law will also determine the parameters of the relationship with Europe and the West generally. In an increasingly small and interdependent world, CIMEL operates as a scholarly legal bridge for research and practice at the crossroad of Islam, the Middle East and the West.